

TOWARD STABILITY AND PROSPERITY

**A PROGRAM FOR RECONSTRUCTION AND RECOVERY
IN KOSOVO**

November 3, 1999

**Prepared by
the European Commission and the World Bank
in Support of the United Nations Mission in Kosovo**

ABBREVIATIONS AND ACRONYMS

CA	Customs Administration
CFA	Central Fiscal Authority
CPO	Cash Payment Operation
EC	European Community
FRY	Federal Republic of Yugoslavia
FYROM	Former Yugoslav Republic of Macedonia
GDP	Gross Domestic Product
GSM	Global System for Mobile Communications
IMF	International Monetary Fund
IMG	International Management Group
KFOR	Kosovo Force
MACC	United Nations Mine Action Coordination Center
NATO	North Atlantic Treaty Organization
NGO	Non Governmental Organization
OSCE	Organization for Security and Cooperation in Europe
PTK	Post and Telecommunications of Kosovo
SFRY	Socialist Federal Republic of Yugoslavia
SWG	Sectoral Working Group
UNHCR	United Nations High Commissioner for Refugees
UNIP	United Nations International Police
UNMIK	United Nations Mission in Kosovo
WHO	World Health Organization

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This report was prepared by a team of European Commission and World Bank staff and consultants, in close cooperation with the United Nations Mission in Kosovo, with the support of the European Bank for Reconstruction and Development (EBRD) and the Food and Agriculture Organization (FAO), and with the assistance of the Kosovo Force (KFOR), the International Management Group (IMG), the US Agency for International Development (USAID), UNICEF, the World Health Organization (WHO), other UN agencies, bilaterals, and non-governmental organizations. The European Commission had primary responsibility for the work on housing and institutions. The World bank had primary responsibility for agriculture, private sector development, water and waste management, landmine clearance, education, health, transport and energy. The European Bank for Reconstruction and Development had primary responsibility for telecommunications.

INTRODUCTION

Five months after the end of the conflict, an enormous effort, on the part of both the Kosovars themselves and the international community, will be needed to put Kosovo on the path to recovery and sustainable development. Infrastructure suffered heavy damage, and homes of more than half a million Kosovars are destroyed. Industry is at a standstill and unemployment remains very high. Institutions are functioning poorly.

Much has already been done, under the leadership of the United Nations Mission in Kosovo (UNMIK), by the NATO-led Kosovo Force (KFOR), UN agencies, bilaterals, and non-governmental organizations (NGOs). Equally impressive has been the enthusiasm and the commitment of the Kosovars themselves: houses are being re-roofed and repaired without substantial donor assistance, schools reopened as early as three weeks after the arrival of KFOR troops with unpaid, but highly committed, teachers. But much remains to be done. Addressing the challenges facing Kosovo – reconstruction, institution-building, and transition to a market economy – will require a substantial level of external support to complement the Kosovars' contributions, and to make the region stable and eventually prosperous.

Experience in other post-conflict situations shows that donor assistance has most impact when it is designed and delivered within a comprehensive reconstruction and recovery framework which clearly identifies key priorities for intervention. This Report is a first step in the definition of such a framework for donor support. In a difficult context, where information remains scarce, the authors drew substantially on UNMIK's work, and on assessments made by KFOR, specialized UN agencies, the International Management Group (IMG), and a number of bilateral and non-governmental organizations.¹ The Report will be further refined as more information becomes available. It is also expected that in-depth discussions of the content of this Report will be held with leading Kosovars in the coming months, and that the substance of these debates will be reflected in a new version.

The Report consists of five parts. The first chapter is an overview, which outlines the recovery strategy, sets overall goals and priorities, and provides an estimate of external funding requirements in each sector. The three following chapters describe specific actions that should be undertaken to help Kosovars address the most critical challenges: restarting the economy and support growth and employment, building the institutions that are needed for medium-term stability and prosperity, and mitigating the effects of both the conflict and the 1990s policies. In the fifth chapter, the report discusses key issues for effective implementation. The report is complemented by a series of sectoral annexes, which include a more in-depth analysis of each sector and its specific needs, and a list of actions for urgent support. A final annex identifies actions that require urgent funding (to be disbursed within the next few months), primarily to help Kosovars get through the coming winter and to prepare next year's activities.

¹ The Report particularly benefited from "Kosovo – Report on Pillar IV's Activities", by Joly Dixon (Sept. 28, 1999), and "Kosovo: Building Peace through Sustained Growth – The Economic and Social Policy Agenda", by the World Bank (November 1999). These documents can be consulted at <http://www.seerecon.org>.

I. OVERVIEW

A. BACKGROUND

1. Under the 1974 constitution of the Socialist Federal Republic of Yugoslavia (SFRY), Kosovo (see Box 1) enjoyed a large degree of autonomy as an autonomous province within the Republic of Serbia. This status was removed through constitutional changes in 1989-1990. In the subsequent years a series of so-called “enforced measures” were implemented, which resulted in the exclusion of most Albanian Kosovars from official institutions and economic life. Throughout the 1990s, a severe economic crisis struck the region, and was compounded by the breakup of SFRY, and of the international sanctions imposed on the Federal Republic of Yugoslavia (FRY). In parallel, the political situation deteriorated substantially, and Albanian Kosovars developed a set of parallel structures, financed by both remittances from the diaspora and “taxes” levied locally. In March 1999, after a year and a half of intermittent fighting, and several attempts by the international community to support a peaceful solution to the crisis, NATO initiated a campaign of air strikes. By June 1999, about one million Kosovars had fled their homes and took refuge abroad. In June 1999, an agreement was reached on a settlement by which, under the terms of United Nations Security Council Resolution 1244, Kosovo is to have substantial autonomy and self-government, under UNMIK’s temporary administration.

Box 1: Facts and Figures

- Kosovo has an area of 10,887 square kilometers (one third the size of Belgium). It is a geographical basin, situated at an altitude of about 500 meters, surrounded by mountains, and divided by a central north/south ridge into two subregions of roughly equal size and population.
- Detailed demographic data are not available – but the total 1998 population is believed to have been slightly above 2.2 million people, including 82 to 90 percent ethnic Albanians. A large diaspora, mainly in Western Europe, plays an important role, particularly through remittances and the financing of the parallel structures developed throughout the 1990s. Minorities include Serbs, Gorans or Bosniacs (Muslim Slavs), Roms, and Turks. Demographic growth is estimated at about twenty per thousand and average household size is believed to be about 6 to 7 persons. Kosovo’s population is by far the youngest in Europe, with about half the people below the age of 20.
- Kosovo is divided into 29 municipalities and about 1,500 villages. It is mainly rural, with about two thirds of the population living in villages, and only nine towns with over 20,000 inhabitants (about 30 percent of the population).
- Pre-war GDP is unknown, since official estimates (at about US\$400 per capita) did not account for a large share of the economy: the informal sector activities. Still, Kosovo was clearly by far the poorest part of FRY.

2. The conflict took a heavy toll on Kosovo. The formal economy is at a standstill, and, in spite of the vibrant restart of informal activities in the trade and services sectors, unemployment is widespread. Many institutions have been dysfunctional for the last ten years as a result of the “enforced measures”, and the conflict aggravated this situation. Physical and human damage are

widespread, resulting from both the last months of fighting and the preceding decade of neglect and lack of maintenance (see Box 2). The Reconstruction and Recovery Program will have to address all of these issues in order for Kosovo to become stable and prosperous, and to be a positive force in the South Eastern Europe's normalization process.

Box 2: The Extent of the Damage

The conflict most severely affected housing, agriculture, and telecommunications. About 30 percent of the housing units, both urban and rural, are unusable. More than 50 percent of agriculture assets were reportedly damaged or lost. Key parts of the telecommunications system were destroyed during the conflict. In addition, equipment of all types and personal property were looted extensively.

But physical damage goes much beyond such direct destruction. Infrastructure networks suffered from a decade of lack of maintenance. Rehabilitation costs will be much higher than preliminary assessments of conflict-related damage alone suggested. The "human damage", resulting from both the conflict and the decade under "enforced measures", is widespread, in particular among the younger generation, which has not had proper access to secondary and higher education.

Most institutions have virtually collapsed. In the immediate aftermath of the conflict, most Serb Kosovars left their (often key) positions in utilities, industry or administration. Archives and technical documents often disappeared in the process. Albanian Kosovars subsequently reclaimed these positions (which they had often held before 1989) – but specialists and skilled workers are still in short supply.

Lastly, little has been done over the last decade to prepare for the transition to a market-oriented economy.

B. MOVING FORWARD – HELPING KOSOVARS HELP THEMSELVES

3. Kosovo's future lies with its full reintegration within the region, through both adequate infrastructure linkages and convergence of economic policies. To achieve economic recovery and growth, the basis of the economy will also need to shift from a system managed under the principles of Yugoslav-style socialism to a market-driven economy relying on private initiative for growth and development.

4. Kosovars are already actively rebuilding their lives and their economy. But substantial external support will be needed to ensure recovery and the development of an open and transparent economy in the medium-term. Donor financial assistance, estimated at US\$2.3 billion, on highly concessional terms, will be required to support a 4- to 5-year Reconstruction and Recovery Program (see Table 1). In implementing this Program, the main challenge will be to address in parallel urgent issues and medium-term requirements. This will require ensuring that emergency assistance is provided in ways that support the necessary institution building, that adequate market-oriented policies are developed to encourage private sector participation in the reconstruction effort, and that a proper balance is struck between speed (for which a hands-on approach will often be needed) and sustainability (which requires the involvement of local authorities and specialists). The specific goals of the Program are three-fold:

- **To develop a thriving, open and transparent market economy**, which can quickly provide jobs to a large part of the Kosovar population; this will require restarting the rural

economy, encouraging the development of the private sector, and addressing the issues of public enterprises;

- **To support the restart of public administration and to establish transparent, effective and sustainable institutions**, by strengthening and reforming existing formal and parallel structures, and by developing new institutions where needed; particular focus should be placed on setting up the central institutions that are key for economic recovery, developing municipal governance, and restoring law and order through an effective police and judiciary; and
- **To mitigate the impact of the conflict and to start addressing the legacy of the 1990s**, with a focus on restoring adequate living conditions (and in particular housing repair, local infrastructure rehabilitation, and landmine clearance), rehabilitating the infrastructure networks needed for economic development (telecommunications, energy, transport), and upgrading social service delivery (both education and health).

Table 1: External Financing Requirements (in US\$ million)²

Activity	First Phase (until December 2000)			Second Phase (2001-2003)	Total
	Until March 2000 ³	April to Dec. 2000	Total		
Agriculture	8	86	94	141	235
Private Sect. Dev./Industry	16	104	120	110	230
Institutions	15	35	50	50	100
Housing	36	270	306	214	520
Water and Waste	30	49	79	181	260
Landmine-Clearing	7	14	21	9	30
Education	11	38	49	36	85
Health	16	24	40	45	85
Telecommunications	15	26	41	54	95
Energy	51	78	129	281	410
Transport	12	57	69	96	165
Subtotal	217	781	998	1,217	2,215
Budgetary Support ⁴	68	60	128	TBD	TBD
Total	285	841	1,126	1,217	2,343

² Estimates are expected to be further refined as more information becomes available and policy discussion evolves. These estimates do not include humanitarian requirements.

³ These requirements correspond to urgent activities, which are further detailed in Annex 11.

⁴ Budgetary support will be needed to finance a deficit, currently estimated at US\$48 million for 1999 and US\$80 million for 2000 (including US\$20 million for the period January to March 2000). Budgetary support requirements for the period 2001 to 2003 are not yet known.

5. Estimates for each phase correspond to the amounts expected to be committed during this period.⁵ In each sector, they include only external financing requirements for investments and technical assistance. In most sectors, substantial operating expenditures will also need to be financed to ensure proper operation or service delivery. However, to make it possible to best allocate scarce resources and ensure that they are directed to highest priorities, to minimize coordination costs, and, most importantly, to link expenditures and revenues, *operating cost support should be channeled through the budget, and ad hoc assistance should be avoided*. This budget, which has been prepared by UNMIK with support from the International Monetary Fund (IMF) and the World Bank, will eventually be funded through local revenues (which UNMIK has restarted collecting), but during a transition period donor support will be needed to finance, on a gradually diminishing basis, a part of the requirements (estimated at US\$48 million for the remainder of 1999 and US\$80 million in 2000).

6. About US\$2.1 billion was pledged at the July 28, 1999 Donor Conference organized in Brussels by the European Commission and the World Bank. Some US\$1.5 – 1.6 billion of this support was directed to humanitarian aid requirements, of which a significant portion has been spent both inside and outside of Kosovo. The remainder of the pledges were targeted to finance early rehabilitation and reconstruction activities, to support Kosovo's budget and civil administration, and to fund peace implementation activities. Set against the requirements of US\$2.3 billion for reconstruction, institution building and budget support, this leaves a significant gap. To ensure rapid implementation, donors are encouraged to make use of lessons learned in other post conflict situations (see Box 3).

Box 3: Key Principles for Designing Assistance Projects in Post Conflict Situations

- Donor effort should seek to complement Kosovar initiatives rather than replace them, and donor funding should leverage local resources wherever possible (in particular, by mobilizing remittances from the diaspora);
- Private initiative should be encouraged and supported, and donors should make maximum use of Kosovars' entrepreneurship; in particular, goods and services should be procured locally whenever possible, to support the restart of Kosovo's private sector;
- Cost-effectiveness is critical, and programs ought to be judged primarily on the basis of their economic viability; cost recovery mechanisms should be implemented wherever possible and appropriate;
- After the coming winter, the transition between emergency humanitarian assistance and recovery should be carefully managed, in particular to prevent providing disincentives for people to return to work (and for farmers to restart their activities) and to ensure a minimum level of support to the most vulnerable; and
- Careful attention should be paid to the sustainability of donor-funded activities, which will require the close involvement of local authorities and technical specialists in a decision-making capacity, as soon as possible.

⁵ For the urgent phase (until March 2000), commitments should be rapidly followed by actual disbursements.

C. THE CONDITIONS FOR SUCCESS

7. Successful implementation of the Reconstruction and Recovery Program will require that a number of conditions are met, including:

- *A macro-economic framework conducive to growth should be further developed and implemented.* Key aspects include: (i) preparing and executing a budget to ensure proper funding of operating expenditures across sectors; (ii) levying taxes to cover Kosovo's financing needs and rapidly substitute donor funding of operating costs – and designing these taxes so as to provide incentives for the restart of economic activities; (iii) establishing a functioning payment system as soon as possible; (iv) reviewing trade policies, to prevent the distortions which are likely to emerge because of the differential treatment between Kosovo's neighbors; and (v) developing an adequate banking supervision framework, to enable the financial sector to play its role in the recovery effort.⁶
- *The legal and regulatory framework should be clarified, and enforcement ensured.* Lasting uncertainties about applicable laws and regulations and their enforcement will seriously jeopardize economic recovery. In some of the most important sectors, substantial support to recovery will not be possible until pending legal questions are resolved (e.g., private sector development, agrobusiness, telecommunications).
- *Kosovars should be closely involved early on in the further design and implementation of the Reconstruction and Recovery Program,* since the eventual success of the economic recovery rests with them. Donors should do as much as possible to ensure that Kosovars, both at the central and at local level, are associated with the preparation and implementation of the projects they finance, in a decision-making capacity whenever possible.
- *Donor financial support should be provided at an adequate level and in a timely manner,* with a view to ensure that policy measures and project activities are well sequenced, and that parallel action is being taken to meet the most urgent needs and to pave the way for sustainable recovery over the medium term.

⁶ Also see “Kosovo: Building Peace through Sustained Growth – The Economic and Social Policy Agenda”, by the World Bank (November 1999).

II. SUPPORTING GROWTH AND EMPLOYMENT

8. Kosovo was traditionally the poorest and least developed part of the SFRY. Throughout the 1990s, the region was struck by a severe economic crisis, with GDP contracting by 50 percent between 1990 and 1995, falling to less than \$400 per capita by 1995 (see Box 4), and unemployment reportedly rising as high as 70 percent. The underlying causes of this crisis (lack of competitiveness in a changing international environment and economic sanctions on FRY) were further compounded by the so-called “enforced measures”. Facing hardship, Kosovars adjusted to the situation in three main ways: (i) emigration, mainly to Western Europe, building up a diaspora which may play an important role in the region’s economic recovery; (ii) return to rural areas, which resulted in more than a doubling of the active population in the agriculture sector between 1990 and 1997; and (iii) development of a large “gray” economy (i.e. informal activities of a legal nature), and of some “black” activities (of an illegal nature).

Box 4: Kosovo’s GDP in 1995

- Industry: 34 percent (predominantly electric power, mining and metallurgy, construction materials, and agroprocessing).
- Agriculture: 29 percent
- Trade and retail: 11 percent
- Construction: 9 percent
- Other: 17 percent (transport, services, etc.)

9. The conflict has taken a heavy toll on all economic sectors. And, despite an impressive restart of small-scale trade and services, productive activity is extremely limited throughout the region, both in the agricultural and in the industrial sector. The current economy consists of three basic components:

- *A multiplicity of small private family farms*, providing some income to about sixty percent of the population. Farm assets have often been lost or destroyed, and most rural households are resorting to humanitarian aid and remittances for their survival (agricultural activities currently makes up only an estimated 11 percent of household income).
- *A relatively large number of privately-owned enterprises*, mainly in the trade and services sectors. Activities have rapidly restarted over the last months, but, in the absence of business regulations, they are mainly taking place within the informal economy.
- *About 200 publicly-owned enterprises*, including 66 “large” enterprises, mainly engaged in mining and metallurgy (in particular the Trepca mining complex), production of raw materials and semi-finished products (lead, coal, zinc and some textiles) – but also agro-business and construction. Most of these enterprises are in poor condition and are not operating.

10. As other Central and Eastern European countries, Kosovo will have to address the challenge of transition to a market-driven economy. In this process, the foundations of the economy are likely to shift from large, publicly-owned enterprises to small and medium private companies, from heavy industry to services, and from essentially traditional agriculture, marked by small farm size and low productivity, to more modern, less labor-intensive agriculture. Experience also shows that resources allocated (often on political or social grounds) to support

non-competitive industries often could have been used in more productive ways (in terms of generating both growth and employment) by supporting market-driven segments of the economy. *Efforts should therefore not be aimed at reestablishing what existed, but at supporting the development of those activities that will most contribute to sustainable growth, both in rural and urban areas.*

11. One of the major concerns in the immediate future is the high level of unemployment, although its impact on the people of Kosovo has, until now, been somewhat mitigated, thanks to both remittances sent by the diaspora and the large amount of humanitarian assistance provided under the leadership of the United Nations High Commissioner for Refugees (UNHCR). Employment opportunities are most likely to be generated through a conjunction of reconstruction activities and private sector development. Special attention should be paid, however, in the design of specific projects, to encouraging labor-intensive schemes (e.g., to rehabilitate rural infrastructure).

12. Donor support for promoting growth and employment should be aimed at:

- Jump-starting the rural economy, to help provide job opportunities in the countryside (both in the agricultural and non-agricultural sectors), relieve pressure on cities, and gradually diminish the need for food aid;
- Encouraging the development of private enterprises, either newly-created or emerging from the informal economy, particularly in agro-business, construction, and services; and
- Assisting in restarting viable publicly-owned enterprises, through privatization.

A. JUMP-STARTING THE RURAL ECONOMY

13. Before 1989, Kosovo was undergoing a transformation from a predominantly rural society to a more urban one – and the portion of the active population engaged in agriculture had fallen to about 26 percent. But, throughout the 1990s, after a number of industrial workers and employees lost their jobs, the rural population increased substantially. In 1998, agricultural activities, together with forestry and agrobusiness, accounted for about 60 percent of employment, and played a key role in food security at the household-level. Agriculture was largely based on small family farms and productivity was low. Typically, farming provided about half of family income, the other half coming from both remittances and off-farm incomes.

14. Today, agricultural production and related processing industries have almost come to a standstill. The 1999 spring cropping season is largely forgone, livestock has been lost or killed (e.g., 50 percent of cattle, 85 percent of poultry), farm mechanization has been damaged (e.g., 55 percent of tractors), many farm buildings have been destroyed, agro-processing equipment has often been looted or made unusable (in particular at privately-owned small and medium enterprises), and housing and rural infrastructure have suffered severe damage.⁷ Kosovo relies heavily on commercial imports and large-scale donor assistance to meet its food demand.

15. The impact of the conflict is compounded by the legacy of the 1990s. Throughout the decade, formal services (e.g., veterinary or advisory services) were not available for the pre-

⁷ Source: World Bank/Food and Agriculture Organization survey of damage in the sector.

dominantly privately-owned farms, access to farm inputs (e.g., fertilizers) was severely limited, investments were curtailed, and major irrigation schemes developed in the 1970s collapsed. On the other hand, Kosovars developed informal parallel structures covering a wide range of agriculture services (such as for input and mechanization supply, or processing facilities). These structures, which were marked by an impressive capacity for private initiatives, are now coming into the open and could be a key factor in driving rural recovery.

16. Rapidly restarting the rural economy is essential to provide employment, income, and food security to rural households. In the long run, growth and employment will be driven by both the development of non-agricultural activities, and the re-orientation of agriculture towards activities in which Kosovo farmers may have a comparative advantage and possibly compete internationally (i.e., labor-intensive cultivation of fruits and vegetables, and some livestock production, rather than grain and industrial crops). But such developments will require a considerable amount of time. In the meantime, and in the absence of any real alternative, agriculture will remain key to providing income and food security for the majority of the rural population, as well as raw materials to the agroprocessing industries. In this first phase, growth in the sector will mainly come from widespread increases in farming production.

17. Donor support should aim both to re-launch agriculture and to address, from the outset, key institutional and structural issues for non-agricultural activities to develop. In addition to the emergency support currently provided by a number of humanitarian agencies (including seeds, fertilizers, and fuel), substantial external assistance, estimated at US\$230 million, will be needed to: (i) jumpstart agricultural activity by helping Kosovars to reconstitute lost or damaged farm assets; (ii) support private sector development in rural areas; and (iii) develop suitable institutions in the agricultural sector. Complementary actions in the housing and rural infrastructure sectors (e.g., schools, electric power supply, health centers, and roads) will be needed – to provide both employment opportunities and basic services to the rural community.

Jump-Starting Rural Activity Through Reconstitution of Farm Assets

18. Given the extent of damage in the rural sector, substantial assistance will be needed to help Kosovars reconstitute their agricultural assets (both livestock and farm mechanization).⁸ Self-help should, however, play a key role in this effort and, although most support should be provided on a grant basis, efforts should be made to leverage local contributions. Support should be provided on the basis of a set of criteria, including the capacity to use assets effectively, and the inability of recipients to fully finance such assets by themselves. To the extent practical, a voucher-based delivery system should be introduced to provide farmers with some choice and increase private sector involvement in the delivery of goods and services.⁹ Where vouchers are not feasible, in-kind distribution should be considered. The distribution process should be managed, under UNMIK's auspices, in close consultation with local communities at the village and municipal level. Due to the absence of formal administrative structures in the field, significant NGO involvement, both international and local, is likely to be required for the implementation of these activities.

⁸ Donor funding is also needed to help re-equip the veterinary system that is now de facto privately operated.

⁹ Vouchers would be distributed to selected beneficiaries and could be used to purchase agricultural equipment from private suppliers (who would be repaid by the donors involved in the scheme).

19. In parallel, key irrigation infrastructure should be rehabilitated, to allow for early recovery of some high value crop production. Full rehabilitation of irrigation systems will require a comprehensive feasibility study and careful analysis of the economic viability of proposed investments, as well as substantial structural reforms to improve management and maintenance of the infrastructure. But in the short-term, some urgent repair of critical parts and structures as well as cleaning of some key sections is required before the next irrigation season.

Supporting Private Sector in Rural Areas

20. Well-sequenced donor support is needed to help in the transition to a market economy and in the development of non-agricultural employment in rural areas:

- *Disincentives to farming should be removed*, as the food security situation improves, by increasingly targeting and eventually phasing out (within 18 months) donor-funded food aid (social protection schemes should be developed in the meantime to support the most vulnerable households). Similarly, donor-supplied farm inputs (seeds, fertilizers, agro-chemicals) should be phased out to prevent the crowding out of private initiative.
- *Financial services should be developed*, to meet two types of needs: (i) credit, for private commercial farms and small scale private agro-processing to finance reconstruction, new investments, and working capital (since transaction costs are high, specialized institutions should be set up, following models developed in other transition countries); (ii) microcredit, for both farm and non-farm investments, and saving facilities for small deposits by rural households; such services require very particular delivery mechanisms, and can best be provided through non-bank financial intermediaries (e.g., a rurally-based microfinance institution). Steps should be taken to initiate both types of institutions, within a sound banking regulatory and supervision framework.¹⁰
- *Socially-owned agro-processing enterprises should be privatized*, as soon as the necessary political consensus is reached, possibly through simple tendering procedures aiming at local investors (also see below, Part C). In a second phase, access to credit resources should be provided (within a sound financial sector framework), to rebuild and/or expand operations and to provide working capital. Technical assistance may also be needed to help in selecting new technologies, or to improve management and marketing.
- *Land and real estate property rights should be secured*. Legislation pertaining to property rights, transactions, and registration should be reviewed and amended, to allow for the development of a secure land and real estate market that is trusted (amongst others) by credit institutions. Non-registered property titles should be formalized, through a several-year, region-wide effort, and the corresponding land registration systems should be developed.

Developing and Strengthening Institutions

21. A new set of policies and institutions should be developed for the sector, both to provide farmers with the framework they need to perform and consolidate the transition to market-oriented agriculture. A minimal agricultural administration should be established, with public

¹⁰ Such a framework has been developed by UNMIK, and is to be implemented in the near term.

involvement strictly limited to a few core functions (e.g., agricultural statistics, quarantine facilities, policy analysis and formulation), and staffing kept at minimal levels. A forestry administration should also be set up to manage existing forests and prevent their further degradation. New legislation should be prepared and passed, in particular with regard to: (i) cooperatives and associations, to allow for the voluntary development of producer cooperatives and professional associations, which are important ingredients of a functional rural economy; and (ii) maintenance of price and trade policies which ensure efficient markets and the free flow of internal and external trade. Technical assistance will be required to prepare such legislation. Higher level agriculture education should be re-established, and an applied research and training system should be supported, in order to increase productivity in the sector.

B. ENCOURAGING THE DEVELOPMENT OF PRIVATE ENTERPRISES

22. The 1990s saw substantial development of the private sector in Kosovo. After ethnic Albanians lost their jobs in socially-owned enterprises, many found alternative income sources in small- and medium-size private sector activities, both formal and informal. In 1996, the private sector contributed 47 percent of GDP and played an overwhelming role in the agriculture, construction, and trade sectors – and it survived better than public enterprises the economic crisis of the 1990s (output levels remained more or less stable).

23. The conflict took a heavy toll on many private enterprises. But, despite the loss or destruction of assets, the restart of private sector activities has been remarkable, in particular in the retail and services sectors, demonstrating an exceptional sense of entrepreneurship by the Kosovars, as well as the availability of small amounts of start-up capital (provided in large part by the diaspora). This process should be firmly encouraged, since newly-created small and medium enterprises have proven to be the main source of growth and employment in most transition economies. In addition to retail and services, short-term growth is likely to come largely from agriculture and agroprocessing, construction, and the production of construction materials – all sectors which are already overwhelmingly private.

24. Substantial donor support, estimated at about US\$205 million¹¹, should aim to lessen the main constraints to private sector development, and in particular to: (i) support UNMIK in designing an adequate regulatory framework; (ii) design and implement mechanisms for providing access to capital for private sector enterprises; and (iii) encourage foreign investment in Kosovo.

Setting the Legal and Regulatory Framework for Private Sector Development

25. The regulatory framework for private business in Kosovo is currently based on FRY commercial law,¹² but in practice it is not enforced (with the exception of the new customs, sales and excise tax regime). The absence of a legal framework may have played a role in the rapid restart of activities, but it denies the economy effective instruments for its further development, and it creates a vacuum which is favorable to illegal or criminal activities. The challenge will be to strike a balance between different objectives: (i) establishing a framework which provides the proper legal basis for sustainable private sector development (e.g., protecting private property

¹¹ As part of the amount mentioned under “Private Sector Development” in Table 1. The remaining portion corresponds to the activities needed to restart (and privatize) viable public enterprises.

¹² As per UNMIK regulation 1999/1.

rights, allowing for the practice of collateral for lending, making it possible to develop venture capital funds, etc.); (ii) providing incentives for the “gray” economy to join the formal sector and, as a result, ensuring a clear separation between “gray” and “black” activities, and (iii) developing a tax basis. Although regulations are needed in a variety of areas (e.g., registration systems, property rights, bankruptcy, contractual law, competition, accounting standards), efforts should be made to keep them minimal and to implement them in a well-sequenced manner, so as not to hinder current private sector growth.

26. The trade and tax regimes should also be refined, so as to provide an environment conducive to private sector growth. In particular, attention should be paid to the cumulative effect of the various fees and taxes on private business. The trade regime could also be adjusted to best support private sector-led growth in Kosovo (e.g., a rebate system could be introduced to stimulate processing, sub-contracting and consignment deals).

Improving Private Enterprise Access to Capital

27. There is currently no bank operating in Kosovo, nor is there a functioning payment system. As a result, private sector activity is limited to areas requiring relatively low levels of up-front investment and working capital – while the economy is strictly operating as a cash commerce system, with all of the limitations of such a system. The absence of reliable payment and credit mechanisms also makes it difficult and expensive to channel donor support to enterprises. There is a consensus that the development of a properly regulated financial sector is of utmost importance for the restart of the economy, and UNMIK is committed to help make it happen quickly.

28. In the meantime, donors may consider supporting lines of credit programs to small and medium enterprises. In the absence of a functioning banking sector, such programs may have to be implemented through a special purpose institution. To ensure proper donor coordination, UNMIK has formulated a set of basic principles for lines of credit, including that: (i) lending activities must be conducted within the new banking supervision framework and in such a manner that supports the medium-term institution building needs for the banking sector;¹³ (ii) credit should be extended only to private enterprises which belong to the formal sector, based on a sound credit analysis, and with due attention paid to fairness, effectiveness, and sustainability; and (iii) borrowing terms should not distort competition with commercial credit.

29. Grant support to enterprises should in principle be avoided, since it is likely to generate distortions and to strengthen resistance against structural reforms. In selected cases, ad-hoc assistance may be the only option at this early stage, but attention should be paid to ensuring fairness, effectiveness, and sustainability. As soon as credit becomes available, grant support should be discontinued – and donor resources should be redirected to more effective types of assistance.

30. SME support programs could be complemented through interventions similar to those which have been implemented in other transition economies, and in particular: (i) business advisory services, to strengthen the business community’s skills (e.g., for developing sound business plans, preparing credit applications, or ensuring proper accounting and auditing); and (ii)

¹³ Also see “Kosovo: Building Peace through Sustained Growth – The Economic and Social Policy Agenda”, by the World Bank (November 1999).

venture capital funds, to increase the amount of resources available for equity investment (these programs could also be very useful in channeling diaspora capital to legitimate investments).

Encouraging Foreign Private Involvement

31. Foreign private involvement in Kosovo's economy could make an important contribution to employment and growth, in particular through subcontracting of labor-intensive activities to Kosovar companies, and direct investments in large enterprises. But current legal and political uncertainties substantially limit Kosovo's attractiveness for investors. As a prerequisite, an investment law, encompassing several basic principles (e.g., protection of investors' rights, non-discriminatory treatment for foreigners and locals, and access to fair arbitration), should be designed and enforced.

32. But in view of the current legal and political situation in Kosovo, even a perfect foreign investment law would not suffice to bring in the amounts of foreign investment needed to make a substantial contribution to growth and employment (and in particular to privatize at least some of the large enterprises successfully). Political risk insurance schemes should be developed, possibly through a cooperation between donors and the private insurance market (e.g., based on what is being done in Bosnia and Herzegovina). Such cooperation would both limit the amount of donor funding required and introduce the private market to Kosovo, thus ensuring a larger degree of sustainability.

C. RESTARTING VIABLE PUBLIC ENTERPRISES

33. Public enterprises were in crisis throughout the 1990s,¹⁴ and output levels dropped dramatically across all industrial sectors (by up to 90 percent between 1990 and 1997 in several key sectors). The difficulties were compounded by the so-called "enforced measures", the lack of investment, and the merging of many companies into Serbian enterprises. Today, with only a few exceptions, Kosovo's 200 public enterprises are at a standstill, and in relatively poor shape. Monetary assets have been taken, equipment is outdated and often inoperative, and most would need significant investment and working capital to be able to produce at any level. Markets have been lost, both in the Balkans as a whole and in FRY. And, after ten years of exclusion, both management's and workers' skills are severely out of date, having missed both the first years of transition and the technological revolution of the 1990s.

34. In addition, the current ownership situation is unclear. In many cases the measures enforced throughout the 1990s have resulted in competing claims between the former workforce (who claim that "social ownership" equaled "ownership by the workers"), and various individuals or companies (who claim that they acquired shares, or that the Kosovar enterprise was integrated into theirs). In some cases, the situation is further complicated by commercial contracts or concession arrangements with foreign companies. Generally speaking, the larger the enterprise, the higher the degree of complexity of the ownership situation.

¹⁴ Unless otherwise indicated, the terms "public enterprise" and "publicly-owned" are used throughout this report to mean socially-owned enterprises as well as other forms of state ownership such as enterprises wholly-owned by the state and joint stock companies majority-owned by non-private shareholders.

35. Any attempt to re-start public enterprises must address the underlying ownership and efficiency issues and create effective corporate governance. To that effect, UNMIK intends to transfer ownership of the public enterprises into private hands.¹⁵ Donor support, estimated at about US\$25 million¹⁶, will be needed, to help design and implement a phased program:

- A set of policies and regulations should be developed to provide an adequate framework for the transfer of ownership of public enterprises, and an environment conducive to effective operation and development of privatized enterprises. In parallel, a public debate should be initiated on privatization.
- A program of selective sales should be launched as soon as possible for small and medium public enterprises in the two sectors with the highest near-term potential for growth: agro-business (around 35 companies) and construction materials (about 20 companies). Most enterprises in these sectors are simple operations of relatively modest size (typically the local brick factory or the dairy plant), with a relatively clear ownership situation, and they often can be re-started through domestic resources (both in terms of investment and management). Such restart is critical, both for the restart of agriculture activities, and for reconstruction. Sales could be conducted through an auction mechanism, with a percentage of the shares kept for the workers.
- Large-scale privatization could follow, as soon as an adequate consensus has been reached (which may not be possible prior to the elections). Large enterprises will need substantial investment, modern management, and access to export markets to restart their activities, which may require involvement of foreign investors. Ownership issues in these enterprises are also often complex. The privatization process could include three steps: (i) UNMIK could establish as soon as possible a mechanism to deal with the various competing claims; (ii) both to strengthen the consensus on the overall approach, and to allow for a rapid restart of the best large enterprises, a pilot program (including about 10 enterprises) of privatization through tenders to strategic investors (with some provisions for worker rights) could be launched, within the next 6 to 12 months; (iii) if this pilot is successful, a second group of enterprises could be privatized under a similar program. Assets of the enterprises which would not find an acquirer should be disposed of as quickly and efficiently as possible. The remaining small and medium enterprises could be privatized through local auctions.

¹⁵ See “Kosovo – Report on Pillar IV’s Activities”, by Joly Dixon (Sept. 28, 1999).

¹⁶ As part of the amount mentioned under “Private Sector Development” in Table 1. The remaining portion covers the support to private sector enterprises.

III. DEVELOPING EFFECTIVE INSTITUTIONS

36. Experience in other post-conflict situations shows that the eventual success of recovery efforts, and of donor assistance, critically depends on the (re)establishment of an effective public administration, both at central and local levels, to design and implement key policies – but also to sustain the effort, maintain reconstructed facilities, and operate restored systems. A combination of issues will have to be addressed:

- The region has inherited institutional structures marked by Yugoslav-style socialism. It now has to face the challenge of transition, as have many other Central and Eastern European countries. New institutions will have to be developed to meet the needs of a market economy, and existing structures will have to be reformed and rationalized, to improve their effectiveness and reduce their costs.
- Kosovo's administration was integrated within the Yugoslav system and key decisions were prepared and made in Belgrade (even more after 1989). The *de facto* large autonomy the region currently enjoys forces it both to develop new structures in key areas (e.g., for policy design), and to revise the internal functioning of existing institutions.
- But Kosovo also has to cope with the legacy of the 1990s. The so-called “enforced measures” resulted in considerable loss of skills and effectiveness, and, combined with the economic crisis weakened substantially many institutions. In addition, the largest part of the population stopped relying on official structures. Informal, parallel institutions were developed in a number of sectors (e.g., education, health, agricultural services), with financing from the diaspora. The current status of these institutions is unclear – and they have to be mainstreamed, reformed, or abolished.
- Lastly, as a consequence of the conflict, most formal institutions collapsed over the last months. A large share of the staff left Kosovo. Documents and archives were destroyed or lost. Equipment was looted. And many public buildings suffered substantial damage. De facto institutions were created, with no legality and sometimes dubious legitimacy, to fill the vacuum – and these also have to be dealt with.

37. Over the last months, UNMIK has established its presence in the field, at central as well as increasingly at local level. Strategies, however, need to be developed early on in all key sectors to allow for the gradual development and empowerment of Kosovar institutions. In most cases, a balance has to be struck in day-to-day activities, between speed, which may require in some cases an interventionist approach to meet urgent needs, and sustainability, which requires that Kosovars be involved in a decision-making capacity.

38. In a complex political environment, flexibility will be key, and adjustments will be required throughout the implementation process. Estimates of the external financial support needed to ensure the development of an effective public administration, at about US\$100 million, are still very preliminary. Additional assistance, which is beyond the scope of this program, will also be needed to support the development of a democratic governance framework (e.g., financial assistance to free and independent media). Donor support for developing effective institutions will be needed in three main areas:

- *Helping set up key institutions of economic management at the central level;*

- *Supporting proper administration at municipal level; and*
- *Assisting in developing a professionalized police and an independent and effective judiciary*

A. SETTING UP KEY INSTITUTIONS OF ECONOMIC MANAGEMENT

39. The proper functioning of a market economy in Kosovo requires the establishment and/or the strengthening of a number of key economic institutions. In most cases, these institutions will have to be started or restarted from scratch. Detailed needs will be identified over time, as implementation of the reconstruction and recovery program proceeds. Based on current knowledge, early priorities have been identified. Donor financing is needed to support provision of technical assistance (for the design, and first phase of operation, of most institutions), training, supply of equipment (e.g., vehicles, computers). Key institutions include:¹⁷

- *A Central Fiscal Authority (CFA) that will perform essential functions of a finance ministry, including: (i) formulation and monitoring of an overall fiscal strategy in light of macroeconomic conditions; (ii) coordination of the public expenditure program and control and execution of spending under this program; (iii) formulation of tax and customs policy and administration and control of the revenue collection. The CFA will be comprised of four main divisions (tax, customs, budget planning and treasury) and an internal audit function. Each department will initially be headed by foreign experts. International advisors have been seconded to UNMIK to staff the budget and treasury divisions. The setting up of the CFA is critical for making it possible to channel donor budgetary assistance and ensure adequate financing of operating expenditures.*
- *A Banking Agency, to ensure proper supervision of the banking sector (and in particular to prevent the emergence of improper banking practices), and help develop a sound financial sector. This agency will be responsible for: (i) licensing new banks; (ii) permitting banks to engage in new activities or offer new products; (iii) permitting merging of banks; (iv) providing guidance to banks on what the supervisor deems to be unsafe or unsound; (v) assessing the condition of individual banks and of the banking system; and (vi) initiating, pursuing and following up on corrective actions.*
- *A temporary facility, the Cash Payment Operation (CPO), is urgently needed to remedy the absence of functioning payment system. The CPO would both execute budget expenditures (salary payments and the like) and receive cash from the customs administration.¹⁸*
- *A Customs Administration (CA), to collect revenues at the border (currently the only source of revenues for Kosovo budget). The CA started its operation in early September*

¹⁷ Also see “Kosovo: Building Peace through Sustained Growth – The Economic and Social Policy Agenda”, by the World Bank (November 1999).

¹⁸ The lack of identification papers currently hampers effective payment for stipends and salaries for public employees, and will become an increasingly important issue for future payment procedures. Immediate steps should be taken to speed up the process of providing personal identification documents to the population (whose previous documents were often confiscated or destroyed during the conflict).

1999, with substantial support from the European Commission. Customs controls were established in key crossing points with the Former Yugoslav Republic of Macedonia (FYROM) and Albania (but several secondary border crossing points remain to be covered). The CA remains understaffed (with less than forty customs officers, while up to eighty would be needed).

- In addition, support will be needed to help re-establish the *Centers for Social Work*, which are delivering social assistance, and in particular to assist in assessment and registration of social assistance beneficiaries, and administration of benefits.
- Lastly, a *series of sectoral institutions* (e.g., education and health administrations, utilities, environmental protection agency) require substantial strengthening. Specific requirements are discussed further in each sector – but external assistance will often need to be accompanied by substantial reforms.

B. SUPPORTING PROPER ADMINISTRATION AT MUNICIPAL LEVEL

40. The rapid re-establishment of functioning municipal institutions is a priority. Municipal authorities have an important role to play in many sectors – including local services (e.g., water supply, solid waste collection, local roads maintenance), education, and health. They also constitute one of the key elements for ensuring proper involvement of Kosovars in the design and implementation of the reconstruction program. But the situation remains difficult: public buildings were damaged during the conflict, archives and documentation have been lost or destroyed, pre-conflict staff (often Serb Kosovars) have left, and, in many instances, self-proclaimed mayors have taken office, without formal recognition.

41. But developing a functioning administration in each of the 29 municipalities of Kosovo raises a number of difficulties, both conceptual and practical. UNMIK is committed to organizing municipal elections as early as possible, which would help establish legitimacy. Beyond the elections, a strategy for developing effective municipal governance needs to be developed – and work is underway to define options for donor support to local governments. In this process, best use should be made of lessons learned in other countries (see Box 5).

Box 5: Remarks on Municipal Institutions Development

- Technical assistance programs have to be kept flexible, to adjust to local circumstances (which may substantially vary from one municipality to the other) and changing needs;
- Foreign involvement should be kept minimal, and aim to strengthen local authorities and to prepare for self-government;
- Elected authorities should be made responsible for the development of their municipalities; they should be closely involved in the selection of priorities, the design of assistance programs, and the implementation whenever possible;
- Urban and rural municipalities have very different needs and capacities, and support programs should reflect these differences.

42. Still, it is already clear that donor support will be required, in particular:

- *To train public officials* – possibly through twinning arrangements with foreign cities, which could second staff to assist newly-elected Kosovar authorities, or receive Kosovar administrators to help them (re)develop their skills; in principle, training programs should be demand-driven;
- *To provide equipment* – and in particular basic office equipment; several implementation mechanisms could be designed to that effect, ranging from a direct supply of equipment to vouchers (distributed based on both the size of the municipality and the level of damage) which may be more effective; close monitoring and supervision will be required, possibly through NGOs or twinned municipalities; and
- *To rehabilitate buildings*, which have often suffered from both the conflict and a decade of neglect; IMG is conducting a detailed assessment of the needs, which should be available by December 2000; rehabilitation works should typically be carried out by local enterprises, possibly contracted through international NGOs.

43. Local governments' operating costs should be covered through the budget – possibly through block grants from the center. Initially only priority expenditures would be covered, but after the elections, municipalities are expected to be granted the authority to levy some taxes, which and should use these revenues to complement central subsidies.

C. ENSURING AN EFFECTIVE JUDICIARY SYSTEM AND THE RULE OF LAW

44. Enforcing the rule of law in Kosovo is essential, both for political stability and economic recovery. After an initial period of lawlessness, during which criminal activities were contained only thanks to KFOR's efforts, the region is gradually returning to some normalcy. Crime has substantially decreased, and, at least in the main cities, some sense of security has been restored. But there are also worrying reports about the development of organized illegal groups, possibly linked to criminal networks in neighboring countries or in the diaspora.

45. UNMIK has appointed a number of judges to try the most serious legal cases. Four district courts and four district prosecutors are currently operating (in Prishtine, Prizren, Mitrovica, and Peje). In addition, a court of final appeal, an office of the public prosecutor, an advisory judicial commission, and a technical advisory commission have been established at the central level. But much remains to be done beyond these emergency measures. The challenge is now to develop an effective judiciary system, conforming to democratic norms and standards, while ensuring the proper functioning of the newly-established institutions in the meantime.

46. In addition, the United Nations is staffing a United Nations International Police, to help restore law and order throughout the province in the short-term. But to ensure the proper rule of law over the medium-term, two critical issues have to be addressed: (i) a democratic and effective 4,000-person strong Kosovo Police Service has to be established – which will require training, equipment, and financing of salaries; similarly, has to be put in place; these efforts are expected to be completed by 2004; (ii) once this force will be operational, a proper and effective transition will have to be ensured between the current, emergency system (in which the United Nations International Police plays a key role), and the longer-term structures.

47. Donor assistance will be needed to finance the setting up of local police and judiciary, including through:

- *Training of Kosovar judges and police*; training programs for judges and prosecutors are currently being developed; in parallel the Organization for Security and Cooperation in Europe (OSCE) has opened a training center for police in Vushtrin, and about 200 officers are already attending a five-week session, to be complemented by in-field training with the UN International Police; 800 more officers are expected to graduate by Spring 2000.
- *Some building construction and or rehabilitation*; courts are in need of repair and refurbishing; police stations were targeted by NATO and suffered heavy damage; and the only jail in Kosovo (in Istok) requires urgent work for minimum human rights standards to be met; IMG is conducting a detailed assessment of these facilities and is expected to make a detailed assessment available by December 1999.
- *Equipment and vehicles*; uniforms, weapons, communications equipment, basic office supplies, and vehicles have all to be provided; a list of the needs for the local police has been prepared by the UN International Police Commissioner; donations should be directed to the Kosovo Police Service and closely coordinated by the UN Commissioner, to prevent gaps or duplication.
- *Operating costs*; donor funding will be needed to finance both wage and non-wage expenditures through the budget; wage levels should be consistent with public service salaries.

IV. MITIGATING THE IMPACT OF THE CONFLICT AND THE LOST DECADE

48. Kosovo needs substantial rehabilitation and modernization. Conflict-related damage has to be fixed, the effects of a decade of neglect have to be dealt with, and effective sectoral institutions and policies have to be developed. Kosovars have already made an impressive contribution to the reconstruction effort. Many observers familiar with other post-conflict situations have been struck by how much the people have already achieved without substantial external assistance, especially in the fields of housing, utilities, and social services, and these efforts must be built upon. For the Reconstruction and Recovery Program to be eventually successful, donor assistance will be required in support of three main objectives:

- *Assisting Kosovars in restoring satisfactory living conditions throughout the region, in particular through housing repair, local infrastructure rehabilitation, and landmine removal;*
- *Rehabilitating the infrastructure needed for economic recovery, in particular the telecommunications, energy, and transport systems; and*
- *Restoring and improving the delivery of social services, namely education and healthcare.*

A. HELP KOSOVARs RESTORE SATISFACTORY LIVING CONDITIONS

49. A large number of Kosovars no longer have homes, and live in tents or with families or friends in overcrowded housing units. Many no longer have proper access to adequate utility services, including drinking water. And the presence, or perceived presence, of landmines throughout the region prevents many from restarting normal activities. Both for humanitarian reasons, and to create the conditions for medium-term stability and prosperity, the donor community should help Kosovars restore satisfactory living conditions through:

- *Rehabilitation of the housing stock, with a view to ensuring “primary rehabilitation” (roof and walls) of most inhabited units by the winter of 2000 – 2001; attention should be paid to targeting scarce assistance to those most in need of it, and to leveraging Kosovar resources wherever possible and appropriate;*
- *Repair of local infrastructure, so as to ensure restoration of basic infrastructure and utilities throughout the region; efforts should be made to design decentralized, demand-driven schemes, which best address the needs of local communities; and*
- *Landmine clearance throughout Kosovo, aiming to clear most minefields by 2002; support should build on the impressive results achieved so far and continue being closely coordinated.*

Housing – Targeting Assistance and Leveraging Local Resources

50. The private housing stock, in both rural and urban areas, has been severely depleted (see Box 6), particularly in the Western part of Kosovo, around the cities of Pejë (Pec) and Gjakovë (Dzakovica). Significant repairs were carried out throughout the summer by the Kosovars, without substantial donor assistance. Still, a large number of people in Kosovo will have to face

the coming winter in destroyed or heavily-damaged housing units, and continued support should be provided over the coming months, to the UNHCR-led winterization program.

Box 6: Quantifying Housing Damage

In July 1999, IMG surveyed about 206,000 housing units in Kosovo (corresponding to the largest share of the existing stock). About 120,000 were reported damaged or destroyed, with a further breakdown into four categories.

Damage Category	Consequence	Percentage of Housing Stock
No damage	No damage	42 percent
I and II	Repairs needed	20 percent
III	Not usable	15 percent
IV	Beyond repair	23 percent

About 500,000 people can no longer inhabit their homes (categories III and IV), and are thus most exposed to winter. The cost of restoring a 75 square meter inhabitable space in each damaged unit was estimated at over US\$1.1 billion.

51. Beyond the emergency phase, substantial and frontloaded donor assistance, estimated at US\$520 million, will be needed to allow for the primary rehabilitation of most inhabited units by winter 2000 – 2001, and to ensure sustainable recovery of the sector over the following years. Since donor resources will, however, not be sufficient to cover all needs, a few guiding principles for targeting assistance should be followed to ensure fairness and transparency:

- Significant local resources have already been made available by Kosovars themselves for housing reconstruction. Assistance should complement, rather than substitute these efforts, and in particular aim to leverage local resources (both labor and financial resources), e.g., through self-help mechanisms. Emphasis should be placed on the provision of building materials (rather than on the financing of works), possibly through vouchers, and effective participation of the beneficiaries should be sought.
- A large number of people do not have access to sufficient resources to repair their houses. To maximize the impact of donor funding (and prevent substitution effects), assistance should be targeted based on both household income and level of damage (with a focus on IMG Categories III and IV), and concentrated in areas where people are already living or have clearly demonstrated their intention to live. Under UNMIK's auspices, a set of guidelines and criteria for selecting beneficiaries should be developed, and practical mechanisms for identifying the corresponding households (possibly through Kosovar and international NGOs) should be set up. It should also ensure adequate coordination to minimize gaps and overlaps.
- In the absence of proven implementation mechanisms, a variety of approaches should be followed, both to reduce the overall risk of the program and to make it possible to identify best practices. Program design should be sufficiently flexible to allow for adjustments

based on lessons learned during implementation. To ensure fairness and consistency, minimum and maximum rehabilitation standards should be developed.

- Procurement arrangements should be designed to foster the restart and development of local enterprises in the construction sector (e.g., through a preference system for local suppliers and contractors).

52. Additional support, mainly in the form of technical assistance, will be needed to ensure the sustainability of reconstruction efforts. An adequate framework for re-registering property rights needs to be developed where ownership titles were lost or destroyed (so that housing units can be used as collateral, bought and sold). Cooperative laws should be passed to allow for changes in the management of collective housing – a pre-condition, in Kosovo as in other parts of Central and Eastern Europe, for good maintenance and improvement in urban living conditions. Lastly, rural migration to cities should be monitored, and urban regulations prepared and passed wherever needed to allow for proper city development.

Local Infrastructure – Supporting Decentralized and Demand-driven Projects

53. Throughout Kosovo, water supply systems are often dysfunctional, whether in terms of quantity or quality (see Box 7), solid waste accumulates uncollected, electric power outages are frequent, and rural roads are not maintained. Restoring local infrastructure is clearly critical. Efforts are needed not only to repair conflict-related damage, but also to partly compensate for a decade of neglect and for the lack of effective institutions.

54. Support is urgently needed to finance relatively small projects that should be implemented before the winter. Detailed project proposals are available with IMG, UNMIK, and KFOR, and include mainly: (i) financing salaries and other operating expenditures of utilities (through the budget); (ii) providing vehicles (particularly for garbage collection, water supply entities, and electricity distribution companies); (iii) supplying chemicals for water treatment; (iv) completing rural well cleaning; and (v) executing minor repair works on rural infrastructure.

Box 7: Water and Waste Management in Kosovo

There are six large water supply systems serving a total of 1,000,000 people – and about a dozen smaller systems, serving 200,000. In rural areas, most households use private wells or draw water from artesian springs. There was virtually no physical damage during the conflict to water supply systems, but about half of the rural boreholes and wells were deliberately polluted. In addition, water companies lost most tools and equipment they need for maintenance.

There is no wastewater treatment in Kosovo. During the conflict, solid waste collection equipment and vehicles were stolen. Currently, many disposal sites are not properly managed.

55. Donor support, estimated at US\$260 million, will be needed beyond the emergency phase to help restore local infrastructure and utilities to minimal levels, in a sustainable manner. Such levels should be consistent with norms and standards applied throughout South-Eastern Europe and may, in some instances, require the upgrading of 1989 facilities. Goals should include, *inter alia*: uninterrupted supply of electric power and of clean water (at about 100 to 120 liters per person per day, with proper quality standards) to all households, development of a primary wastewater treatment scheme in the Greater Prishtine (Pristina) area, proper garbage collection and disposal in all major cities, and adequate road access to all villages in Kosovo. To ensure proper operation and maintenance of the restored infrastructure and facilities local utilities or

technical entities will have to be strengthened and re-equipped. Three types of projects need to be prepared throughout the winter, for implementation beginning in Spring 2000:

- Where major rehabilitation works are needed, specific sectoral projects should be designed and implemented – including, (i) for the five largest water supply and waste water systems, (ii) for large-scale delivery of garbage collection trucks, and (iii) for rehabilitation of the electric distribution network. These projects should include a strong institutional component, including both provision of equipment and technical assistance where needed to allow the existing entities to adequately maintain and manage rehabilitated infrastructure. UNMIK is expected to provide a framework for the definition of such projects, in particular by setting or endorsing priorities.
- In rural areas, the necessary works are often very small-scale. Experience shows that involvement of local communities in small infrastructure repair is critical to success. Donors are encouraged to adopt demand-driven approaches, to ensure Kosovar participation, and to develop decentralized implementation mechanisms, which best respond to each specific challenge.¹⁹ UNMIK should coordinate these efforts, to prevent project duplication and ensure that selection criteria are consistent across donors.
- In the cities, comprehensive city revival programs should be developed, particularly for the three cities that suffered the most severe damage (Pejë, Gjakove, and Mitrovica). Typically, these would focus on repairs to municipal infrastructure, but they could also include other initiatives (for example twinning with foreign cities) aimed at revitalizing these urban centers through a set of cultural activities or other events.

Mine-Clearing – Continue to Support the MACC-Coordinated Effort

56. The presence, and the feared presence, of landmines has considerably hindered return to normal life. The magnitude of the problem, however, is somehow limited, compared to other affected regions. There are about 1,000 identified minefields in Kosovo, and about 230 casualties have been recorded to date (out of which 40 were fatal). If financing remains at current levels, the landmine and unexploded ordnance problem could be eliminated within the next three years.²⁰

57. Considerable mine-clearing capacity (16 NGOs and private companies, totaling almost 600 staff) has already been deployed, with impressive preliminary results. Effective coordination by the United Nations Mine Action Coordination Center (MACC) has been key to success and donors are encouraged to explicitly request their implementation agencies to work within the framework defined by the MACC. In the next phase, external financial support estimated at US\$30 million is needed, with a focus on:

- *Improving the existing data base* set up in July 1999. All suspected areas should be systematically verified, mapped and marked (about 30 percent of accidents have happened

¹⁹ Specific projects have been developed by both the European Commission and the World Bank.

²⁰ Except possibly for minefields located along the borders and around Yugoslav Army compounds (about 20 percent of the suspected minefields), which are expected to be cleared by the Yugoslav Army – no schedule is available yet.

in non-registered minefields), and the available information should be broadly disseminated to local communities.

- *Continuing the current clearance effort*, and, to maximize its impact, developing an adequate prioritization process, which would make it possible to concentrate capacities in critical areas. The MACC is committed to rapidly setting up such a process which would also make it possible to require clearance in support of specific recovery projects (to facilitate implementation, some of the clearance effort may be embedded in other programs, typically by adding a mine-clearing component to an infrastructure project).
- *Supporting mine awareness*, through both formal and informal education. This has proved to be the most effective way to prevent casualties, in particular among children. Providing assistance to mine victims, is also critical, typically by improving emergency medical treatment, providing prostheses, and ensuring that social benefits are available.

B. RESTORING AND UPGRADING SOCIAL SERVICES DELIVERY

58. Many schools and health facilities were damaged or destroyed during the conflict. But the education and health sectors also suffered severely throughout the 1990s (see Box 8). Being de facto excluded from the formal education and health systems as a consequence of the so-called “enforced measures”, Albanian Kosovars developed parallel structures to deliver these services. Under these circumstances, remarkable results were achieved – life expectancy and infant mortality did not deteriorate substantially, and primary education enrollment ratios remained at around 90 percent. But despite Kosovars’ efforts, there was only so much that could be achieved. The health status of the population remained in the lower range of European standards (e.g., infant mortality at about 50 per thousand live births). Secondary education, as well as higher education, deteriorated substantially (in spite of the efforts of both teachers and students), and a large portion of youth could not get adequate qualification.

Box 8: Kosovo’s Education and Health Systems

Education. Until 1989, Albanian Kosovars could benefit from education in their language, and enrollment was quasi-universal. After 1989, FRY authorities reasserted control over education content in 1990, and Albanian Kosovars left the formal education system and developed a “parallel system”. Under this system, primary education was often delivered in official schools – but teachers were neither recognized, nor paid by the Serbian Ministry of Education. Secondary and higher education were often delivered in private houses, with police forces harassing both teachers and students. Primary education enrollment ratios were reportedly kept above 90 percent, until the first massive population movements in 1998, but were significantly lower for secondary education. About 30 to 50 percent of school facilities suffered substantial damage.

Health. As in other parts of FRY, health services were delivered in Kosovo through a public, excessively specialized system – including a tertiary hospital in Prishtine, five district hospitals, polyclinics, and small primary health care clinics – financed by pay-roll and profit contributions to a health insurance fund. After 1989, many Albanian Kosovars lost health insurance fund coverage. A parallel system was set up, to provide primary health care through the Mother Theresa Society and other services through private practice. About 700 doctors and 1200 nurses graduated from a parallel training system. In the official system, there was little investment, with adverse effects on quality. During the conflict, many Mother Theresa Society clinics were destroyed, while hospitals and polyclinics suffered little damage.

59. Since June, Kosovars have demonstrated their commitment to restoring and upgrading delivery of social services: schools have restarted with unpaid teachers, and medical care is being delivered. But much needs to be done to help Kosovars make up for the lost decade and remedy the impact of the conflict. Substantial donor assistance, estimated at US\$85 million for the education sector and US\$85 million for the health sector, will be necessary, in particular to: (i) help mainstream parallel systems; (ii) finance operating costs (through the budget) during a transition period; (iii) restore damaged facilities and replace lost equipment; (iv) assist in designing and implementing specific remedial programs; and (v) support the transition to modern education and health systems.

Mainstreaming the Parallel Systems

60. Developing an effective institutional framework for the delivery of education and health services is obviously critical. Efforts should build upon the achievements of the 1990s, and in particular aim to mainstream the informal education and health parallel structures. UNMIK has a key role to play in this effort, and, beyond the emergency phase, should no longer focus on directly administering the systems, but rather help Kosovars in adjusting their structures and incentive mechanisms to improve the management of the sectors:

- In the education sector, the parallel system has come out into the open and is in effect the only system. Main issues include restoring adequate funding mechanisms, redefining the respective roles of the central administration and the teachers, and ensuring quality throughout the system. To that effect, focus should be placed on defining an adequate, decentralized financing mechanism, as described below, and on providing the right incentives for the system to gradually modernize. In parallel, support should be provided to the central administration for a series of core functions (e.g., definition of curricula, quality control, evaluation of system/student performance).
- In the health sector, the parallel system has virtually collapsed. Since June, most medical staff who worked in the Mother Theresa Society's dispensaries have tried to return to the hospitals where they worked before 1990, and, as a result, the Mother Theresa Society system functions poorly if at all in many areas (in particular in the countryside). Efforts should focus on maintaining adequate service delivery, and in particular primary health care in rural areas. Medical practitioners and nurses should be discouraged from returning to over-staffed, over-specialized hospitals, and UNMIK should provide financial incentives to work in primary health care centers, in particular in rural areas.

Financing Operating Costs

61. Adequate financing of operating costs (both wages and non-wage expenditures) is the most critical requirement in the social sectors. Most donors have focused their assistance on physical repairs or provision of emergency supplies, but few have responded to what sector professionals perceive as the greatest need: the payment of salaries. Although most Kosovars have, until now, accepted resuming work without being paid, this situation is clearly unsustainable. Support for non-wage recurrent costs (e.g., drugs, heating) is also necessary. UNMIK began to pay stipends to education and health sector workers in September 1999, and these payments must be continued. As in other sectors, operating costs should not be financed on an ad hoc basis, but through the budget.

62. To maximize the effect of these contributions, an adequate governance framework should be put in place. As a first step, to the extent possible, decentralized mechanisms should be set up

for the management, operation and financing of the social sectors. In principle, a two-tier structure should be adopted: (i) primary education and primary health services should be operated by local governments, with (in a first phase) block grants provided by the central authorities for their financing; central authorities should concentrate on ensuring universal coverage and minimum quality standards and evaluating performance in the system; (ii) the higher level system of education and health should be financed from central revenues (with gradually increasing user fees for services such as student dormitories at the university).

63. Efforts should be made to rapidly ensure the self-sustainability of the health sector's recurrent expenditures, through both the revitalization of the Health Insurance Fund and the development of user co-payments. Technical assistance is urgently needed for the redevelopment of the Health Insurance Fund, to help restart raising revenue (through pay roll and profit contributions), to train staff (budgeting, resource allocation, monitoring and control), and to prepare for medium-term reforms and improvements.

Rehabilitating Damaged Facilities

64. Donor support is also needed to restore damaged facilities and to replace lost or destroyed equipment. A large number of organizations are already at work to meet the most urgent priorities and this effort should be continued and expanded. Before financing large rehabilitation works, donors should, however, ensure that the restored facilities will meet the needs of the new health and education systems. Typically, secondary and higher education are likely to undergo significant reform over the next few years and the type of facilities or equipment required may be very different from that which was available before the conflict (and which often dated from the pre-1989 period). At the university (which currently functions as a loose association of independent faculties), improving the efficiency of management should be a pre-requisite for major donor investment. Similarly, there may be a need to group together several dispensaries in some rural areas, and to restructure, and often downsize, hospitals. To guide donors, WHO has produced interim policy guidelines for investment in the health sector. Similar guidelines should be rapidly prepared for the education sector. UNMIK should closely coordinate donor efforts to maximize the use of scarce resources. A detailed assessment of education and health facilities, their current status and the related needs, is expected from IMG by the end of December 1999.

Supporting a Series of Remedial Programs

65. Substantial support should also be provided to mitigate the impact of "invisible" damage. Although much attention has been paid to destroyed or damaged infrastructure, the consequences of a decade of "enforced measures" have been severe on individuals. Special programs should be supported, and in particular:

- *A series of remedial education programs*, including: (i) basic literacy and skills training, in particular for young people (often girls in rural areas) who did not have adequate access to education; (ii) job training for people aged 15 to 25 who have not received proper professional education (and who constitute a potential source of civil unrest) – with a focus on high demand activities (e.g., construction); (iii) skills upgrading for those who could not benefit from a fully satisfactory higher education, in particular among university students; and (iv) new skills development, in particular in those fields that are most critical for a market economy (e.g., management, finance, accounting, computing). Donors should support the creation of a re-training fund, both to address these needs and to provide a medium-term framework for adult training. This fund should be managed by a board made up of government, business, education and union leaders. Potential suppliers

(academic, private sector, NGOs, etc.) would be expected to submit proposals for training delivery. Based on an agreed set of criteria, the board would select projects to be financed through the fund.

- *A series of priority health programs* for improving the overall health status of the population, by addressing major health-related issues, including post-conflict trauma, reproductive health, mental health, community based rehabilitation, tuberculosis control, diabetes and renal disease prevention and management; in addition, arrangements need to be made to ensure adequate provision of services previously delivered in Belgrade (e.g., oncology).
- *Professional training for education and health personnel*; a series of specialized programs, building on similar programs in neighboring countries, should be developed to update and improve professional skills, after a decade of isolation.

Assisting the Modernization of the Social Sectors

66. Lastly, donor assistance will be needed to help manage the transition from current structures, basically still inspired by Yugoslav-type socialism, to more modern systems, in line with both market economy requirements, and current practices throughout the European continent. Key aspects of the transition will include:

- *In the education sector:* (i) a model of education governance and financing, in which budgetary programming and expenditure control is devolved to municipalities, while a central ministry takes responsibility for establishing broad standards, monitoring system performance and ensuring quality; (ii) a central curriculum, reflecting European best practices, should be developed, together with a capacity for evaluating student achievement; a particular focus needs to be given to child-centered teaching methodologies; and (iii) new broad-based secondary programs need to be developed to replace traditional, occupationally-specific programs, and the secondary teaching force needs to be re-trained.
- *In the health sector:* (i) re-establishing the policy and planning functions, and revitalizing the institutes of public health; training and technical assistance will be needed to enable Kosovar authorities to oversee health strategy and service delivery; (ii) reviewing and clarifying the legislative framework and governance arrangements for health insurance, public health regulation and health service delivery.

67. Experience in other countries suggests, however, that, whenever they can be delayed, key policy decisions should not be made until Kosovar education and health experts have had a chance to study what has been done throughout the 1990s in other countries which had to face similar problems. In the coming period, donors should help Kosovar specialists catch up with the latest innovations, trends, and developments in their sector, typically through exchange programs and study tours.

C. REHABILITATING INFRASTRUCTURE NETWORKS FOR ECONOMIC RECOVERY

68. With the exception of telecommunications (and some road bridges), infrastructure networks suffered relatively little direct conflict-related damage. But lack of maintenance has

been pervasive over the last decade, and, due to the departure of a large portion of qualified staff, technical institutions and utilities are not functioning. Restoring adequate telecommunications services, energy supply, and transport capacity is a pre-requisite for economic recovery.

69. In view of the nature and the scope of the investment required, donors should design their support with a view to medium-term sustainability. In particular, efforts should aim to re-establish functioning infrastructure to the level required for sustained economic recovery (rather than limit assistance to repairing what existed before the conflict, which was already deteriorated compared to the pre-1989 period). Kosovars should be involved, in a decision making capacity, wherever possible, both in needs definition and in actual project implementation – since they will be responsible for operation and maintenance over the next decades.

Developing Sustainable Institutions and Financing Systems

70. Across all infrastructure sectors, adequate systems should be rapidly set up, to manage, operate and finance the systems. Donors should assist UNMIK in developing and implementing a set of policies, in particular to:

- *Transfer management to Kosovars.* Most infrastructure and utilities are currently managed by KFOR or by foreign specialists engaged under concession or management contracts. Beyond the emergency phase, management responsibility should be transferred to Kosovars as early as possible. The role and legal status of utilities and infrastructure management companies should be clarified, and management teams should be appointed and empowered. Training should be provided to both younger employees and to those who have spent the past ten years out of the office. UNMIK should gradually restrict its role to designing and implementing a solid financing and regulatory framework in all these sectors.
- *Restructure utilities and infrastructure management companies.* The current institutional vacuum, and the fact that most potential workers in these companies have not worked there over the last ten years, offers an opportunity to restart these institutions on the right foot. UNMIK and donors should not support the re-establishment of the pre-1989 structures where they are ineffective. In particular, attention should be paid to prevent overstaffing, since staffing needs are only a fraction of 1998 levels. UNMIK and donors should encourage Kosovars to rapidly adopt the principles of modern infrastructure and utilities management.
- *Promote private sector delivery.* Throughout the 1990s, a number of private enterprises were developed to provide alternative services delivery, where public enterprises were not effective or competitive (e.g., for public transportation). This development should be encouraged wherever possible, and in particular, in the fields of public transport, telecommunications, and road maintenance. But it should also be accompanied by the development of an appropriate regulatory and supervisory framework – for which UNMIK will require substantial donor-financed technical assistance.
- *Develop sustainable financing systems.* In the coming years, donors will have to finance capital investments, including working capital. But cash expenditures for operation and maintenance should be financed from user fees as soon as possible and certainly as soon as systems are functioning normally (with lifeline tariffs to allow for the most vulnerable households to meet their basic needs). Adequate revenues should also be collected

through the budget as early as possible, to cover other financing needs (e.g. fuel taxes should be raised for funding road maintenance).

Restoring Telecommunications Service

71. With about 130,000 phone lines in service, Kosovo's telecommunication network has the lowest telephone penetration rate in Europe, at about 6 lines per 100 persons (about a quarter of the FRY average of 22 lines per 100 persons). During the conflict, a number of key facilities were destroyed (including the main exchange to the rest of FRY and to the international network, the two transmission stations, and a local exchange in Prishtine). Communications on the fixed network are de facto limited to local calls. International access is not available. And despite the two mobile licenses issued by FRY, there is no mobile service in Kosovo except in Prishtine.

72. Prior to 1989, the entity operating Kosovo's telecommunication network was combined with the postal service. After 1989, there were a series of changes in the institutional structure, including the sale of 49 percent of Telecom Serbia (which had subsumed Kosovo's telecommunications entity) to Telecomms Italia and OTE (the national operator in Greece). UNMIK is establishing a "juridical entity", Post and Telecommunications of Kosovo (PTK), and is giving it the right to operate all present and future telecommunications assets in Kosovo (although it does not confer ownership rights). But a number of regulatory issues remain unresolved. UNMIK will need to play a key role in addressing them, and donors may consider providing expertise in critical areas. Key issues include: (i) to obtain the necessary authorizations to establish international relationships/access to foreign operators; (ii) to give the necessary authorizations to develop a mobile GSM service throughout Kosovo; (iii) to re-establish billing for telephone service; (iv) to reach an agreement for payment of calls to the rest of FRY (and international calls); and (v) to create an entity that can receive donor funding while ownership issues are being resolved.

73. Rapid rehabilitation of the telecommunications network is key for successful economic recovery. In principle, telecommunications is an income-generating activity, and a large part of the reconstruction program could be financed by private operators, in particular the development of a functioning GSM service and most of the expansion of the network. Still, in view of the emergency of the situation, the extent of damage (and the poor development of the network), and the current uncertainties about Kosovo's political status, some donor support will be needed to complement private sector activities. External support, from both donors and the private sector, tentatively estimated at US\$95 million, should be heavily frontloaded, so as to allow for a rapid resumption of telecommunications services. Efforts should focus on:

- Repairing damage to the existing network, including: (i) restitution of long distance microwave network (SDH 6-7GHz); (ii) replacement of Kosovo tandem switch (2,000 trunks) and the Prishtine local exchange; and (iv) repair of local distribution network (including civil works);
- Providing spares, tools, test equipment and maintenance vehicles;
- Carrying out a limited modernization and expansion of the network, to replace obsolete analogue exchanges by digital ones, double the network capacity, and establish an international access for Kosovo in addition to that via FRY;
- Ensuring adequate mobile coverage throughout the region, to meet the demand that cannot be satisfied on the fixed network; and

- Providing technical support to the telecommunications operating entity, whose staff has little experience of modern technology, management, markets and market norms.

74. In view of the urgency of the needs, adequate implementation mechanisms should be designed that would allow early resumption of adequate service, while respecting the interests of the various entities legitimately involved in the sector. An option would be to establish a separate legal entity to receive donor funds and invest in equipment; this entity would then lease or otherwise make available this equipment to the operator of the fixed network.

Improving Energy Supply

75. Energy supply is key for the restart of economic activity in Kosovo – as well as for the Kosovars to get through the cold winter months. But damage has been extensive and the systems function poorly (see Box 9). Urgent measures have been taken, with the award of an international management contract for the electric power sector to operate throughout the winter, and the definition by UNMIK of an emergency program which donors are encouraged to support.

Box 9: Current Status of Kosovo's Energy Sector

- **Generation.** The two main power plants (both thermal) suffer mainly from lack of maintenance. The relatively new Kosovo B (600 MW) is not in operation and requires substantial repairs. The old, environmentally-hazardous Kosovo A (800 MW), has one or two units (out of five) operating intermittently and at reduced capacity. The smaller (35MW) Gazivode hydro power plant can operate at full capacity.
- **Transmission.** The 400 kV connections to Montenegro, Serbia, and FYROM, are out of operation. The 220 kV network is in poor condition, and the restoration of the lines to FYROM and Albania has become critical for network stabilization. Significant parts of the 110 kV ring network are out of service, in particular in the South and South-West of Kosovo.
- **Distribution.** Thirty percent of the network is affected by conflict-related damage. Distribution companies lack tools, vehicles and equipment, which are key for maintenance.
- **Coal.** Two large mines, Mirash and Bardh, provide lignite (of relatively poor quality, but with favorable extraction conditions) to the power plants. There is no conflict-related damage to the mines – but all mobile equipment has been removed. Production restarted in July 1999 (at low levels).
- **District Heating.** The pre-conflict district heating systems – in Prishtine (about 80,000 consumers), Gjakova, Mitrovica and Lipljan –have suffered only minor conflict-related damage, but are not operating due to lack of maintenance
- **Institutions.** There is no adequate institutional framework for efficient operation of either the power and district heating systems or the coal mines: no company structure, no business culture, and no functioning billing and collection service.

76. Substantial donor support, estimated at US\$410 million, will be needed to support the medium-term rehabilitation of the energy sector:

- After Spring 2000, Kosovo B (which will require a major overhaul over the summer of 2000) should function as the primary source of domestic power for the next 15 years. One

unit of Kosovo A should be kept operational to meet the residual demand for another 3 to 4 years. Environmental mitigation measures need to be developed for the two plants. During this period, surveys should be conducted to assess Kosovo's longer-term energy needs and required capacity²¹ (and Kosovo A should eventually be replaced, either by a new power plant or through reliable long-term electricity import arrangements).

- Coal extraction should be rationalized, to provide sustainable coal supply to the power plants, in sufficient quantities and at costs compatible with the requirements of competitive marketing of electricity in the domestic market.
- Concurrently, the transmission and distribution networks should be restored, with an initial focus on principal substations, major transmission lines, and distribution networks (some of these needs may also be addressed through local infrastructure initiatives).
- Lastly, billing and collection activities must restart as early as possible, with a view to finance the operating expenditures in the sector.

Rehabilitating Transport Networks

77. The transport sector is in poor condition (see Box 10), and substantial donor assistance, estimated at US\$165 million will be needed for its rehabilitation.

78. *Road network.* Conflict-related damage was relatively limited (about a dozen bridges were destroyed on the main highways), but the lack of maintenance throughout the 1990s produced deplorable effects. Much urgent work has already been done by KFOR, which re-opened the railways and airport (for military purposes), and put temporary bridges or bypasses into place wherever needed. But large parts of the road network may soon become unusable if the backlog of maintenance is not rapidly remedied. In particular, equipment, salt and sand should be urgently provided to complement KFOR efforts and ensure serviceability of the network throughout the coming winter. Beyond this urgent phase, donor support should be aimed at both rehabilitating the road network over a 4- to 5-year period and establishing adequate construction and maintenance capacity. Priority works include: (i)

Box 10: The Transport Sector in Kosovo

- **About 3,800 km of roads** (including 623 km of main roads, and 1,300 km of regional roads), generally in poor condition, due mainly to a pervasive lack of maintenance throughout the 1990s.
- **330 km of single track, non-electrified railway**, with a North – South line (Belgrade – Mitrovica – Prishtine (Pristina) – Skopje) and branch lines to Pec, Prizren and Podujevo. KFOR has restarted traffic (for its own logistics needs) on the Mitrovica – Prishtine – FYROM line.
- **One airport**, near Prishtine, which suffered heavy conflict-related damage and loss of critical equipment (although civilian flights are expected to resume very soon).
- **A non-functioning public transport system**, which has been partly replaced by private operators.

²¹ Kosovo was a net exporter of electric power, but at prices which did not cover production costs. Such activities should not restart unless a feasibility study establishes their profitability.

permanent reconstruction of all damaged bridges; (ii) patching, overlays, reconstruction, and drainage works on about 450 kilometers of main and regional roads (in order to support their restart, involvement of local companies should be encouraged); (iii) rehabilitation of 400 kilometers of gravel and dirt roads, using labor-intensive methods, to help provide rural employment; (iv) constructing bypasses in key locations (e.g., border crossing point with FYROM); (v) restoration of horizontal and vertical signalization on the main and regional roads; and (vi) provision of essential equipment to local companies (e.g., trucks, earth and overlay works equipment, spare parts for asphalt plants and crushing units), as payment for their work.

79. *Railways.* The need to restart large-scale railway operation will depend on the eventual restart of traffic to Belgrade, as well as on the degree and nature of industrial recovery (in particular in the mining and metallurgical sectors). Until the situation has stabilized, and a feasibility study can be conducted (to assess medium-term traffic perspectives, and identify corresponding requirements), there should be no large-scale investments in the railway sector. A small amount of donor assistance will be needed in the short-term to complement efforts currently underway by KFOR (which is expected to operate the network until at least September 2000), in particular to refurbish and re-equip the main workshop, and to provide some locomotives.

80. *Civil aviation.* Prishtine airport is expected to be re-opened for civilian traffic very soon. Some support will be needed over the coming months to make regular civilian traffic possible, including: (i) supply of equipment, mainly aeronautical ground lighting and navigational aids; (ii) pavement works on the runways; and (iii) training for local staff to eventually take over and run the operations (e.g. air traffic controllers). For the airport to operate under normal conditions, further rehabilitation will be needed, including substantial civil engineering works (e.g., control tower, passenger terminal, etc.) and supply of equipment (e.g., fire fighting vehicles). Such activities should not, however, be undertaken until a feasibility study has been carried out, to assess prospective traffic and identify corresponding priority requirements.

V. IMPLEMENTING THE PROGRAM

81. The scope of the proposed Recovery Program is large, compared to Kosovo's still limited implementation capacity. Implementation will raise major challenges for both donors and Kosovars:

- Reconstruction and rehabilitation of buildings make up a large part of the program. The design of implementation mechanisms should take into account the actual capacity of the rapidly-growing construction sector. The extensive use of self-help mechanisms for the housing program is expected to minimize the need for contractors, and to leave enough capacity for the construction sector to carry out the public buildings programs (institutions, education, health) as well as the remaining part of the housing program (for the most vulnerable). The total amount of the works to be contracted is not believed to exceed the capacities that can be developed during this period. In fact, implementation capacity will be mainly constrained by the availability of sufficient quantities of construction materials: Kosovar capacity is likely to be too limited to meet the needs, and large-scale imports will be required.
- A series of more specialized construction activities will have to take place in most infrastructure sectors (energy, telecommunications, water). For the most complex and most expensive (e.g., power plant overhaul) programs, donors should be encouraged to resort to contracts with reputable international companies or the initial suppliers, to smooth implementation. Smaller works (typically water supply system rehabilitation or road maintenance) will have to be implemented by local enterprises. An effort will be needed to help these local companies develop the necessary capacity (e.g., through provision of equipment as advance payment for services due).
- Large amounts of equipment and supplies (e.g., agricultural assets, garbage trucks, tools) will have to be imported to Kosovo. Procuring goods should not raise significant difficulties, but their transportation and distribution will be challenging. Current bottlenecks should be rapidly remedied (see Box 11).
- Limited institutional capacity (for selection of beneficiaries, implementation of credit lines, installment of equipment, etc.) will raise acute problems. But developing institutions is both a condition for successful implementation and an objective of the program, and it is expected that

Box 11: Two Major Challenges for Implementing the Program

- **The absence of a functioning payment system.** UNMIK is committed to ensuring that such a payment system is rapidly developed, but until such a system is in place, donors may consider making most payments outside of Kosovo – which would require using NGOs or private companies, whether Kosovar or foreign, who have access to foreign bank accounts.
- **A logistics bottleneck at the border between Kosovo and FYROM.** The passage of trucks and supplies through this border should be facilitated, possibly through the opening of inland customs processing stations. Donors may also consider pre-positioning goods, or design projects in ways to minimize the impact of serious logistics delays.

the current weaknesses will be gradually remedied. In the short-term, difficulties can be overcome by: (i) focusing the existing institutions on priority tasks; and (ii) making extensive use of NGOs as appropriate.

82. Implementing such a large Reconstruction and Recovery Program is ambitious, and will only be possible through a major, concerted effort, involving Kosovars, UNMIK, and donors, as well as NGOs and the private sector. Drawing on experience in other post-conflict situations (see Box 12), key aspects of a successful implementation setup can be identified: (i) detailed projects have to be prepared and implemented; (ii) effective donor coordination mechanisms have to be set up, to ensure that synergies can be developed; and (iii) transparency has to be ensured.

Box 12: Lessons from Other Post Conflict Situations

Local Ownership. Program implementation is most effective where priorities for donor assistance are established jointly with the national authorities. Involvement of local stakeholders (including the private sector, local communities, NGOs, etc.) improves efficiency and sustainability.

Donor Coordination. Donor coordination is essential to avoid gaps, overlaps, or inconsistency of policy advice, and to ensure sustainable budget expenditure planning.

Sustainability. Although institutional and policy reforms are generally seen as a secondary priority to physical reconstruction, they are key to recovery and stability. Emergency programs also often fail to take into account the need for funding recurrent costs – jeopardizing the success of investment projects.

A. PREPARING AND IMPLEMENTING SECTORAL RECONSTRUCTION PROJECTS

83. *Preparing detailed sectoral projects (including bills of quantities and specifics on implementation mechanisms) is on the critical path for successful implementation of the Recovery Program.* Experience in other countries suggests that only a few donors will have a project design capacity in the field. Most will rely on local authorities or NGOs to provide them with detailed project proposals, which they would evaluate and possibly finance. But the current institutional capacity in Kosovo is very weak, technical data and documentation are scarce and often incomplete, and most Kosovar experts and specialists have left the region and have not come back yet. At this stage, neither Kosovar technical authorities, nor UNMIK can provide donors with comprehensive, ready-to-be-financed project proposals. And time is running short, since it would require, in most sectors, at least two to three months to prepare such detailed projects. The World Bank and the European Commission are preparing some sectoral projects, which donors are encouraged to consider co-financing. But beyond these efforts, UNMIK should take the lead in ensuring that comprehensive sectoral priority projects of a magnitude consistent with the needs in each sector, are prepared. Efforts should be initiated as early as possible, for a first set of projects to be ready by February 2000, so that donor pledges can be committed for works to start in Spring 2000.

84. In view of the tight timetable, involving Kosovars to the extent desirable in the preparation of the emergency projects may be difficult. As a minimum, the identification and sequencing of specific activities should be discussed with local groups. Consultants should also

be encouraged, wherever possible, to closely liaise with local technical authorities. Beyond Spring 2000, all such consultancy contracts should include a significant training element, to ensure that Kosovars will increasingly be able to relay foreign experts.

85. To implement the projects they finance, donors will undoubtedly use a variety of mechanisms. Although each donor is tied by its internal procedures and often has little room to maneuver, several principles should be followed: (i) Kosovars should be involved as much as possible and as early as possible in the process, and efforts should be made to strengthen, rather than bypass, local technical institutions; (ii) the creation of new structures should be limited to the extent possible; and (iii) projects should be designed in a comprehensive manner, to prevent ineffective use of resources (e.g., supply of equipment with no provision for installation).

86. In most infrastructure and utilities sectors (including electric power, coal mining, telecommunications, transport, water, and waste), assistance should be channeled through the utilities or management entities, with proper oversight arrangements to ensure transparency and effectiveness – and specific implementation units could be created within these entities to ensure a clear delineation of responsibilities. In agriculture, private sector development, support to institutions, education, health, and housing, small central technical units, staffed with Kosovars but supported by foreign consultants, could be established to ensure the coordination of donor-funded activities, which would largely be implemented through NGOs or ad hoc institutions. Mine-clearing assistance should be allocated under the MACC guidance.

B. SETTING UP EFFECTIVE DONOR COORDINATION MECHANISMS

87. An impressive number of aid organizations are already at work in Kosovo. Experience of reconstruction programs in other post-conflict situations shows that a well-functioning aid coordination mechanism is key to successful implementation, and in particular: (i) to direct assistance to priority needs, in a timely manner; (ii) to help prevent gaps or overlaps; (iii) to develop synergies among donors, building on each donor's comparative advantage; and (iv) to reinforce donor influence in the policy dialogue. Four main ingredients are needed: (i) well-defined priorities at the program-, sector- and project-level and appropriate mechanisms for adjustment as program implementation proceeds; (ii) counterparts within the region who have both the responsibility and the capacity to ensure satisfactory program implementation; (iii) a comprehensive, up-to-date, and easily available information data base, on priority investments, donor programs, and overall implementation status; and (iv) "least-cost" coordination mechanisms among donors, in which benefits to all far outweigh costs.

88. To help in this effort, the European Commission and the World Bank are committed to helping Kosovo authorities to mobilize funds and to assess progress on the ground. The European Commission and the World Bank will further refine and regularly update the Recovery Program, organize and co-chair donor conferences, and keep comprehensive records of donor pledges.

89. In the field, UNMIK is expected to provide strong leadership, in close collaboration with Kosovar representatives, to ensure proper coordination of day-to-day implementation, mainly through a series of Sectoral Working Groups (see Box 13). UNMIK is setting up a donor database to monitor the implementation of donor assistance. This database will not only constitute an important instrument for donor coordination but it will also be a critical source of information for budget planning purposes.

Box 13: Sectoral Working Groups

A Sectoral Working Group (SWG) may be set up for each sector (or group of related or similar sectors). Members will include all key actors in the relevant sector(s), including representatives of major donors. A “lead agency” (among the specialized international agencies) will be tasked to provide secretariat to, and help lead, each SWG. SWG will be in particular responsible for:

- maintaining a policy dialogue between UNMIK and donors, to ensure that external assistance is implemented within an appropriate sectoral policy framework;
- coordinating sector-specific policy conditions of donor support;
- keeping abreast of priority investment needs in the sector, and matching projects with donors;
- identifying sectoral funding gaps; and
- monitoring sectoral program implementation.

C. PROMOTING TRANSPARENCY

90. Transparency is essential, both to maximize the impact of externally-funded projects, and to provide donors with a sufficient level of confidence to remain involved over the medium-term. But experience in other post-conflict situations also shows that ensuring adequate transparency is often difficult. From the very start, donors should be intransigent on such issues, and ensure that all partners they are financing, whether local or international, whether governmental or non-governmental, are irreproachable, and in particular have put into place effective audit mechanisms.

91. For donor support channeled through the budget, donors and UNMIK should work together in two fields, to develop an overall framework conducive to transparency:

- All public operating expenditures should be made within the framework of a budget. Transparent procedures should be developed for the execution of this budget – and control mechanisms should be put in place. Key to that effort should be the distinction between the contracting, controlling, and payment functions.
- An independent, external auditor should be contracted both to certify accounts and to ensure a compliance audit (e.g., respect of bidding procedures), for all public expenditures. In the absence of a parliament, the auditor’s reports (typically produced on

a quarterly basis) should be made public. This auditor could provide similar services to those donors which request it (against a fee).

92. For donor assistance not channeled through the budget (and in particular for most of the investment program outlined above), donors are encouraged to follow a set of rules conducive to transparency, including:

- Supporting the setting up of a cash payment office, initially managed under UNMIK's auspices, as well as the development of an appropriate banking supervision framework;
- Setting up special accounts for each project, and appointing auditors to follow up the use of the funds through regular audits of these accounts;
- Using competitive procurement wherever possible, encouraging a broad participation of both local and international contractors, and requiring full disclosure of all information related to the selection of the best bids;
- Designing projects in a comprehensive manner, and in particular, make a provision for the installment of the procured goods, so as to ensure their actual effective use; and
- Making a provision for funding of close project supervision, in particular through regular performance audits of implementing partners.

ANNEX I: AGRICULTURE

A. INTRODUCTION

1. This note (1) aims to provide a concise analysis of the constraints and opportunities facing the rural economy and the agricultural sector in Kosovo in the aftermath of the conflict waged in 1999; and (2) suggests a medium term (four year) program comprising policy actions and public investment recommendations aiming at re-launching the rural economy in Kosovo on a path of sustainable and widely shared growth. Reliable and detailed quantitative information on agriculture in Kosovo has not always been easily accessible, and particularly in the case of conflict damages, not available. The Food and Agriculture Organization (FAO) and the World Bank have therefore commissioned an agricultural damage assessment which was carried out in August and for which first results became available in September 1999¹. This note is in part based on the preliminary results of this agricultural damage assessment survey.

B. THE RURAL ECONOMY AND THE AGRICULTURAL SECTOR

2. Kosovo was always the poorest province of the Socialist Federal Republic of Yugoslavia (SFRY). By 1995, GDP had reportedly fallen to less than US\$400 per capita, with unemployment estimated to be as high as 70 percent. Migration from Kosovo to neighboring countries has been a common survival strategy for many households over the past years.

The Rural Economy

3. Before the conflict waged in Kosovo between March and June 1999 and prior months of rising and often violent tensions in 1998, the rural population accounted for around 65 percent of the total population in the province. An estimated 90 percent of this rural population was engaged in agricultural activities either on a full or on a part time basis in the years preceding the conflict. While detailed demographic data for the province are not very reliable, as of September 1999 the rural population is estimated at around 1,066,000 persons, while the agricultural population accounts for some 1,000,000 persons which represent some 100,000 to 150,000 farm households. In 1997 the 'active population engaged in agriculture' amounted to over 50 percent of the active population (which includes a considerable number of part-time farmers) and around 70 percent of the labor force, if including associated upward and downward linkages as well as the forestry sector. This high share of active population in the agricultural sector has, however, not always been the case. The same source for 1991 records some 26 percent of the active population engaged in agriculture.² The sharp increase of population associated with agricultural activities over the past ten years is due to the fact that many employees lost their jobs and had to return to (often part-time) farming as the means to ensure food security.

¹ See also "Kosovo: Damage and Needs Assessment in Agriculture. Preliminary Analysis". September 20, 1999. A more detailed report based on further survey data processing is currently in preparation and will be made available in due course. The results are based on a sample survey undertaken in 25 out of 29 municipalities in the province during late July and August 1999. The survey comprised two questionnaires, one at the farm household level which was used to interview 1,837 farm households; and a second at the village level which was used to gather information in 163 villages throughout the province.

² Source: Economic Activities and Democratic Development of Kosova. Research report prepared by Riinvest, Pristina, September 1998.

The Agricultural Sector

4. The agricultural sector accounts for a significant share of economic activities in the province. In 1995 the value of primary agricultural production in Kosovo was estimated at US\$213 million, representing 30 percent of provincial GDP, or 35 percent of GDP with the inclusion of forestry and food processing³. These figures are likely to be an underestimate of the full sector output given a considerable amount of unrecorded activities. Kosovo has traditionally been a net importer of food and agricultural products, such as wheat. While part of the agricultural area is fertile and well suited to the production of grains and industrial crops (such as sunflower or sugar beet) it is unlikely to have a comparative advantage in the production of these high volume, low value commodities. Rather, within agriculture the comparative advantage is likely to be in more labor intensive production activities, such as vegetables and some fruits,⁴ and in some livestock production (such as ruminant-based meat and milk production). Kosovo has significant pasture resources which have little alternative use and can provide a low cost production basis for a competitive, forage-based livestock industry. In the aftermath of the conflict and in the absence of significant alternative economic activities in rural areas over the medium term, agriculture is likely to remain an important element of the province's food security, in particular at the household level in rural areas.

5. Kosovo, which embraces about 1.1 million ha, is characterized by four main watersheds rising in a westerly and northerly crescent of mountains, from which rivers run south and south-east to intersect elevated (300-1000 m) and relatively fertile plains. Approximately 430,000 ha is forested (39 percent) and 577,000 ha is classified as agricultural land (52 percent).⁵ Of the latter, about 180,000 ha (31 percent) are pastures and about 400,000 ha (69 percent) is cultivable. Erosion in upland areas and water logging (55,000 ha) are common. The climate is continental in the east with an average 660 mm rainfall and 170-200 frost-free days, but Mediterranean influences in the south-west bring wetter (780 mm) and warmer (196-225 frost-free days) conditions to that area.

6. Approximately 67 percent of agricultural land, including 90 to 95 percent of cultivable land, 30 percent of pastures, and 38 percent of forestland is privately owned. Socially owned *agrokombinats* (18) or agricultural cooperatives (145), established through self-management agreements, control the balance of the non-urban land resource and most medium and large scale agro-industry. Average private land holdings per family are about 3.2 ha, including about 2.4 ha of arable land, often fragmented in 4-6 plots (see Table 1).

³ Source: Economic Activities and Democratic Development of Kosova. Research report prepared by Riinvest, Pristina, September 1998.

⁴ Before 1989, Kosovo was a net exporter of some fruits and vegetables, e.g. to other republics of the Socialist Federal Republic of Yugoslavia.

⁵ Federal Republic of Yugoslavia Yearbook, 1998.

Table 1: Land Use of Private Farms (1997)

	Average Farm Size (ha)	Share of Land (%)
Total Farm Land ¹	3.22	100%
Agricultural Land ²	2.43	75.5%
Arable Land	1.57	64.6%
Pasture	0.73	30.0%
Perennial Crops	0.13	5.4%
Forest	0.79	24.5%

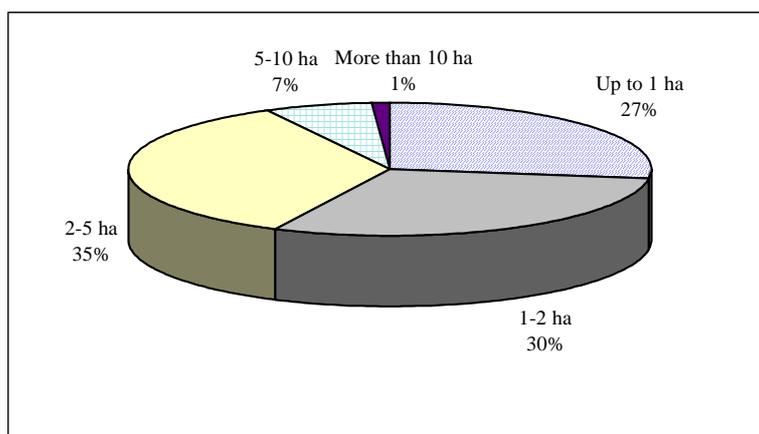
¹ Total farm land = agricultural land + forest

² Agricultural land summarizes arable land, pasture and perennial crops

Source: Kosovo: Agriculture Damage and Needs Assessment in Agriculture, 1999

7. Figure 1 shows the distribution of family farm by size. The farms greater than 10 ha include about 630 medium-scale farms established under private ownership in the 1980s.

Figure 1: Distribution of Farms by Sizes (ha)



Source: Kosovo: Agriculture Damage and Needs Assessment in Agriculture, 1999

8. Before the conflict, around half of family income, on average, originated from farming. The remaining was received in roughly equal shares from remittances and off-farm incomes (small businesses, shops, trade, etc.). In the period from 1997-1999, the share of farm income of overall income decreased, while the share of remittances and aid donations increased (Table 2). For nearly a third (32 percent) of the farms less than 20 percent of their incomes originated from farming activities. On the other end of the spectrum, about 26 percent of the farmers rely for more than 80 percent of their income on agriculture.

9. The importance of agriculture as share of total income decreased sharply over the last three years to around 11 percent in 1999. This is a result of the largely lost cropping season of 1999. Rural families had to rely on remittances and on aid donations to a large extent. Aid donations amount to almost 40 percent of farm household income in 1999. In the present crisis

situation people heavily relying on agriculture can be considered as one of the most vulnerable groups as they missed out at least one year's crop and often lost a large amount of their livestock.

Table 2: Origin of Farm Household Incomes (%)

Year	Income from Farming	Off-farm Income	Remittances	Aid donations	
1997	50.2	25.5	23.7	0.6	
1998	38.4	23.4	26.9	11.2	
1999	11.2	19.8	29.9	38.7	
Share of farm income in total income in 1997	0-20 %	20-40 %	40-60 %	60-80 %	80-100 %
Share of farmers in category in 1997	31.8%	18.3%	13.2%	10.9%	25.7%

Source: Kosovo: Damage and Needs Assessment

10. Of the roughly 400,000 ha of cultivable area in 1997, about 291,000 ha (50 percent of agricultural land) was arable (cropped) land, 86,000 ha was meadows, which are typically lower and wetter than the upland pastures, 12,000 ha was in orchards and 8,000 ha in vineyards (Table 3). Winter wheat and spring barley have been the main food crops, while maize, primarily used for animal feed, has been the other principal crop. Fodder crops, vegetables and industrial crops have also been of importance.

Table 3: Land Use in Kosovo, 1997

Cropped Land	291,000 ha	Wheat	110,000 ha
Meadows	86,000 ha	Maize	95,000 ha
Orchards	12,000 ha	Fodder Crops	36,000 ha
Vineyards	8,000 ha	Vegetables	28,000 ha
Pastures	180,000 ha	Spring Barley	16,000 ha
Total Agricultural Land	577,000 ha	Industrial Crops	6,000 ha

Source: Official Yearbook of the Federal Republic of Yugoslavia, 1998

11. More than one quarter of the cultivable area or roughly 106,000 ha is under irrigation (76,500 ha under managed irrigation schemes and about 30,000 ha of private smallholder irrigation). In 1992, 12 percent of orchards in Kosovo belonged to the social sector and 88 percent have been privately owned. Vineyards were 40 percent socially and 60 percent privately

held. Most production from these lands went to Agrokosovo's⁶ refrigerators, juice plants or wineries, mostly located in the South-west of Kosovo.

12. Livestock form about 50 percent of the value of agricultural production and, in 1997, included about 421,000 cattle, 365,000 sheep, 69,000 pigs, 27,000 goats and 4.5 million poultry. Almost all private farmers kept dairy cattle (on average 1-2 milking cows per farm) and poultry, with much smaller numbers having sheep, goats, pigs and horses. Dairy cattle provided food for the household, especially children, animal manure for crop fertilization and cash through the sale of livestock and some milk surpluses. Sheep and goats also satisfied home needs but produced greater marketable surpluses, particularly of weaned stock and cheese. Poultry predominantly met home needs, commercial production being mostly a social sector activity.

13. Crop and livestock yields in general are low - exemplified by an average wheat yield under 3 ton/ha, and a dairy cattle milk production of about 1,500 l/year. Yields have been falling, together with agricultural GDP, through much of the 1990s, in large part due to reduced access to and applications of agricultural inputs (in particular fertilizers), and agricultural services imposed by FRY authorities. Input supply and product markets, together with some advisory services, were provided by a network of 145 cooperatives and 96 associated trading centers, that (together with important irrigation infrastructure) contributed to raised agricultural production and productivity in the 1970s and 1980s. These cooperatives and trading centers are now defunct while much of the irrigation infrastructure is unusable. While fertilizer use has also been falling in Central and Eastern European Countries (CEEC) as a consequence of economic liberalization in the 1990s and it has started to recover since the second half of the 1990s. With fertilizer applications in 1996 reaching 18 percent of the 1989 levels (or 85 kg per ha of arable land) the decline in fertilizer use in Kosovo, in particular on private farms has been considerably greater than what has been experienced in CEEC countries and may be verging on soil de-nutrition. Veterinary services were provided through 28 municipal veterinary stations which are equally largely inoperational. As mentioned earlier there has been a high increase in labor to the agricultural sector. This has been coupled with an increase in farm mechanization, in particular tractors, by around 40 percent (which have, however, had a significant off-farm use). Overall, total as well as factor productivity (labor, land, capital) has hence fallen over the past decade.

14. The socially owned *agrokombinat* enterprises include two large flour mills, 3 feed mills, about 10 bakeries, 2 export-oriented large animal and 2 poultry slaughter houses, a 100,000 l/day milk processing plant and several smaller dairies, 3-4 fruit juice production plants, one vegetable oil extraction factory, a sugar mill, several vegetable processing units and 5 large wineries. Little primary production is carried out by the *agrokombinats*. Due to poor maintenance and management and a policy of maximizing the supply of products coming from FRY, processing output at these plants during the 1990's decreased to as little as 5 percent of capacity. Private enterprises of much smaller capacity have emerged during the 1990s to partially fill this gap, including about 20 flour mills, 50-100 small bakeries, several semi-private communal slaughterhouses and feed mills and 2-3 small dairy factories. It remains to be seen how competitive the emerging private processing industry will be able to produce within a liberalized economic framework and more stringent food safety and quality requirements.

⁶ Agrokosovo is a *kombinat* holding company, linking 18 smaller *kombinats* in the province of Kosovo.

Conflict Damage

15. As a direct consequence of the conflict, some 75 percent of the rural population was subject to mass migration: some 43 percent of the rural population took refuge abroad and a further 32 percent became internally displaced. By mid-August 1999, around 85 percent of families that had previously left their homes had already returned to their village of origin. As a result of this disruption (and prior months of rising and often violent tensions) agricultural production as well as related processing industries have almost come to a standstill. The spring cropping season of 1999 has largely been forgone and this year's wheat harvest is a fraction of normal levels (45 percent of 1997 production). The province currently relies on commercial imports (mainly from the Former Yugoslav Republic of Macedonia, Albania, Montenegro and Greece) and large-scale donor relief aid to meet its food demands. Affordability and, to a lesser extent, access to key farm inputs (seeds, fertilizers, fuel) remains limited in the province.

16. Farm assets have been damaged on a massive scale in the course of the conflict. The replacement value of losses of animals, destroyed farm buildings, and agricultural machinery is conservatively estimated to amount to around US\$700 to US\$800 million.⁷ The majority of livestock (cattle: 50 percent, small ruminants: 65 percent, poultry: 85 percent) which contributed around half of the value of agricultural production is reported to have been lost or killed. Over half of the agricultural mechanization (tractors: 55 percent, combine harvesters: 75 percent) are lost or need repair. Many farm buildings (stables, sheds and storage space) have been destroyed. While fallow land and the loss of cattle has taken place throughout the province, the loss of agricultural mechanization and farm buildings seems to be more concentrated in the western municipalities. Preliminary results from the agricultural damage assessment commissioned by FAO and the World Bank suggests that the following group of ten municipalities (no ranking implied) has been the most severely damaged:⁸ Decan, Fushe Kosove, Gjakova, Glogovac, Istok, Klina, Mitovica, Peja, Skenderaj, and Vushtriu.

17. Agro-processing equipment, in particular at privately owned small and medium size enterprises, has also experienced significant damage either through direct destruction or looting of assets. The high demand for wood (both for fuel and construction purposes) in the aftermath of the conflict is putting increasing pressure on the longer term sustainability of forests in the province. Village-level infrastructure (schools, drinking water, power connections, health care centers) have equally been damaged or destroyed on a scale yet to be determined. Mines, present or perceived to be present in rural areas, are currently limiting access to agricultural and forest land.

Past Legacies

18. **Backlog on Economic Transition.** Prior to the significant restrictions on the province's autonomy status in 1989, the agricultural sector was subject to numerous economic distortions over a longer period of socialist planning. A system of (partly implicit) subsidies and taxes on various economic activities resulted in inefficient farm structures by 1989. A majority of small family farms (limited by law to 10 hectares) were integrated by contractual arrangements with the large-scale *agrokombinat* and cooperative sector which provided subsidized farm inputs and

⁷ Other sources are putting damages to the agricultural sector in the order of US\$1.5 billion.

⁸ With regard to the *combined* application of the following indicators: livestock losses over 55 percent; functioning tractors lesser than 50 percent; and damage to farm building greater than 65 percent (the latter is based on the EC/IMG household damage survey as proxy for damages to farm buildings).

protected markets for primary produce. Though many instruments of the past economic regime have been largely abolished (for instance, high levels of trade protection and active price policies, input subsidies and subsidized credit), structural constraints persist. At the farm level this is reflected in terms of low labor productivity, small marketable surplus, and limited farm size; and on the part of the processing industries in terms of a privatization agenda for the socially-owned *agrokombinats* and often outdated and uncompetitive technologies.

19. **Decade of Neglect.** The current standstill in the agricultural sector is compounded by some ten years of neglect. Around the early 1990s, key managers and technical specialists in the processing industries and the agricultural administration were replaced. In the following years, the enterprises were poorly maintained. Almost no formal services (such as veterinary and advisory services) were provided to the pre-dominantly privately owned farms. Access to farm inputs (such as fertilizers and agro-chemicals) was severely limited. Investments into farm and processing equipment have been curtailed during that period resulting in an aging of farm machinery assets and the obsolescence of processing technologies. Land markets slid into informality because of high transaction costs, laws that prevented ethnic groups from selling land to each other, and poor performance by land agencies. Two major irrigation schemes constructed in the late 1970s have fallen into disrepair since 1990.

Opportunities

20. **Private Sector Initiatives.** During the 1990s, Kosovar Albanians developed informal parallel structures of considerable extent covering a wide range of agricultural services such as input and mechanization supply, veterinary services, and processing facilities. These parallel structures, marked by an impressive capacity for private initiative, are now coming into the open and will be a key factor driving the recovery of the rural economy and the agricultural sector. A tradition of private family-based agriculture, the presence of an emerging dynamic private sector associated with processing and input supply, and limited reliance on public sector support, all augur well for the re-launching of a rural economy. These represent opportunities that donor-supported activities should build on and seek to complement.

C. RE-LAUNCHING THE RURAL ECONOMY – A MEDIUM TERM PROGRAM

21. In the following section, the note outlines the suggested objectives of a medium term program aiming at re-launching the rural economy. The concrete policies and investments proposed under the program are summarized under three themes: (i) partial reconstruction aimed at jump-starting agriculture and the rural economy; (ii) support to private sector in rural areas; and (iii) support to institutional capacity building.

Objectives

22. The broad range of issues to be addressed – from dealing with the immediate impact of conflict damage, to the consequences of a decade of crisis, to structural issues inherited from the pre-1989 period – require a differentiated approach in terms of objectives and instruments. This program is based on a set of objectives, some of which can be achieved in the near term and some of which are of a longer term nature. A critical challenge for this program consists in ensuring that, by striving for the immediate and short run goals, policies and investments do not jeopardize the feasibility of medium and in particular, longer term objectives. Another major challenge of re-launching the rural economy in Kosovo is that many of the activities associated with medium and longer term objectives need to be initiated already in the immediate future in an environment where institutional and implementation capacity is scarce. While in the longer run the creation of

non-farm employment will be a key determinant of the rural economy in Kosovo in terms of increasing both on- as well as off-farm productivity, this will require considerable time. Until then, agriculture will be key in providing income and household level food security for the majority of the rural population in the province as well as raw materials to the agroprocessing industries (a key source of non-agricultural, rural employment). Without a recovery of the agricultural sector in the short run, migration from rural areas and abandonment of agricultural land can well be the consequence. Therefore, this program recommends a two pronged approach aiming at re-launching agriculture during an initial period while at the same time establishing the framework in which non-agricultural activities will develop. The latter will take many years and will go well beyond the scope of the Reconstruction and Recovery Program.

23. The overall objective is to support major structural changes in the rural economy over a phased transition. The goal here **is not** to restore agriculture to its pre-conflict state, nor to return to the pre-1989 conditions. The scope of damages are too large, and potentially available resources insufficient to allow for a replacement of assets on a large scale. More importantly, farm structures and agricultural production have shown inefficiencies as the result of long term economic policies, and should not be restored to their previous state. Rather the objective **is** in a first instance to support the re-emergence of agricultural production to ensure minimum levels of income and food security to the rural community at large. The number of people affected in rural areas are well beyond what can be sustainably supported by a social welfare program. As an alternative, non-agricultural employment becomes available (in particular for those that were forced into agriculture during the 1990s) and factor markets (labor, land, capital) start functioning, the objective is to reach for productivity gains and structural changes in agriculture and the rural economy. The following outlines the set of objectives – ranging from immediate to long term – that would contribute to reaching the above mentioned goals.⁹

24. In the *immediate term* (the next 6 to 12 months; 1999 to 2000) the aim is to assist the farming community at large (which represent the vast majority of the rural population) to re-start agricultural production in particular during the winter season of 1999 and the spring season of 2000. This should also include a public livestock vaccination campaign against major contagious diseases to help safeguard the remaining animal stock in the province. These activities are currently being addressed on a priority basis by the international community. In particular ECHO, USAID, FAO together with numerous NGOs are providing critical farm inputs (seeds, fertilizer, machinery services, spare parts) on a grant basis to support the planting of the winter wheat crop by October / November of this year. This activity is of a relief nature and aims at providing a limited aggregate supply of farm inputs.¹⁰

25. In the *short run* (the next 6 to 18 months, 2000 to mid-2001) the objectives of public support (both policies and investment) consists in supporting the re-launching of agricultural production on a broader scale with the aim of replacing in aggregate some of the conflict damaged assets (livestock, farm mechanization, farm buildings, irrigation). This would also contribute to the re-establishment of non-agricultural employment in the food processing industries which (amongst others) require raw materials to restart operations, as well as in the upstream farm input services. The support provided would be of a one-time nature with a defined sunset clause.

⁹ While the objectives seem to imply clearly marked phases, in practice the boundaries between the different phases are likely to be blurred.

¹⁰ See also section on Agricultural Relief Operations.

26. In the *medium term* (the next 3 years, 2001 to 2004) the objective of the rural program is to establish the economic framework and instruments which would support employment creation and income generation for a large share of the population in Kosovo through agricultural and non-agricultural investments. The key for supporting the emergence of non-agricultural economic activities is the provision of a sound legal and economic framework. The latter would include the provision of a broad range of rural financial services on a commercial and sustainable basis to support economically and financially viable investments in agriculture, agro-processing and other economic activities in the rural economy. It would also include the registration and protection of private property rights in land and real estate.

27. **Incentives.** Maintaining an open trade regime for agricultural inputs and products is an underlying assumption of this program. An open trade regime for agricultural commodities provides consumers with access to relatively inexpensive food. It also provides farmers and rural entrepreneurs with the relevant economic signals on which to base investment and production decisions. Overall, it contributes to supporting the structural changes aimed for in the rural economy of Kosovo. The aim is to establish an incentive framework that is neutral vis-à-vis the agricultural and food processing sector in that it neither unduly taxes (explicitly or implicitly) nor subsidizes productive activities. The current trade regime levies import duties and taxes on farm inputs while providing duty and tax exemptions for key agricultural commodities (milk, fruit, vegetables, wheat). In addition, agricultural commodities imported from FYROM are being delivered on the basis of a low, preferential import duty (1 percent). Hence, the current incentive regime potentially taxes primary agricultural production. A review of trade policies (including recommendations) is provided in a separate Economic Memorandum currently under preparation by the World Bank.¹¹

Program Summary

28. Based on the previously outlined objectives, a four- to five-year program (until 2004) has been developed, with policies and public investments grouped around **three themes**: (a) partial reconstruction aimed at jump-starting agriculture and the rural economy; (b) support to private sector development in rural areas; and (c) support to institutional capacity building. Activities need to be launched and implemented from the onset across all three areas and hence the areas do not imply a sequencing; rather, the emphasis is anticipated to shift over time.

29. The program aims to be selective, by postponing public investments that are not essential to the re-launching of the rural economy to a later stage, such as the establishment of a large agricultural administration, a public extension service, or land consolidation activities. Also activities that are incompatible with the sustained development of the sector have been excluded, such as financing of socially-owned enterprises or the pursuing of an active agricultural price and trade policy.

30. **Theme 1: Partial Reconstruction aimed at Jump-Starting Agriculture and the Rural Economy.** The emphasis of donor support would be on (a) continuing to provide elements of social protection under World Food Program's on-going food aid program; (b) continuing to provide on a declining scale farm inputs on a relief basis; and (c) partially repairing or replacing conflict damaged assets in agriculture and the rural economy. A full replacement of conflict damaged assets is not an economically viable option. In addition, given the limited absorptive

¹¹ See: Kosovo: Building Peace through Sustained Growth. The Economic and Policy Agenda. The World Bank. November 1999.

capacities within the province and limited donor funding, only assistance for partial replacement of assets is envisaged. At the farm level, assistance would be provided to farm families to obtain or access farm inputs, livestock (cattle) and agricultural machinery (tractors, implements, spare parts). Support would be directed to those heavily damaged farm households which have past farming experience and hence the capability to put farm assets to good use, but which lack the resources to re-establish their asset base by themselves. Partial cost recovery, mostly of an in-kind nature, would be introduced. Recipients will be selected in consultation with local communities at the village and municipal level.

31. Donor supplied farm inputs (seeds, fertilizers, tractor services and repairs) would be converted to a voucher based approach (including targeted allocation of vouchers) and ultimately phased out in the course of the year 2000 to avoid crowding out of private sector initiative in this field. Supply side constraints for farm inputs are rapidly being overcome by Kosovar entrepreneurs.

32. To the extent practical, a voucher-based delivery system could be introduced if appropriate providing some choice to farmers and increased private sector involvement in the delivery of capital goods (farm equipment, cattle) and services. Where vouchers are not feasible, public procurement of goods would be carried out requiring international suppliers to link up with Kosovar dealers with the aim of ensuring local private sector involvement in distribution and after-sale services. NGO involvement, both international and national is required for the implementation of these farm level activities. Some (in-kind) cost recovery would be envisaged, for instance on the basis of asset sharing by beneficiaries at the local community level; however, a large grant element is likely to prevail given family's need to often concentrate their limited earning reserves into shelter and housing.

33. Reconstruction of key irrigation infrastructure allowing early recovery of some high value crop production, and subsequent broader rehabilitation (including institutional reform) of the irrigation subsector is a further element in re-launching the agricultural sector. This would be complemented by the rehabilitation of rural infrastructure (schools, electric power supply, health centers, roads) which would provide employment opportunities as well as basic services to the rural community; an initial funding mechanism is currently being established which will finance small-scale rural infrastructure investments on a grant basis and which is likely to require further financial support.

34. **Theme 2: Support to Private Sector in Rural Areas.** Policies and investment activities under this heading would be initiated early on in the program to ensure the sustainability of the reconstruction phase and the establishment of non-agricultural employment in the rural areas of Kosovo. A first important investment to be undertaken early in the program to ensure animal productivity consists in re-equipping the veterinary stations that are now de facto privately operated, with the aim of ensuring adequate provision of veterinary services while keeping the number of publicly employed veterinarians low.

35. A second critical element in private sector development in rural areas will be the future of the agroprocessing sector at all scales of operations. One important step in this regard is privatization of socially-owned agroprocessing enterprises early in the reconstruction phase (either before or after elections in Kosovo), using simple tendering procedures aiming at local or regional investors, combined with post-privatization financial support to ensure operations of

privatized assets.¹² A second step will consist in providing agroprocessing industries of different scales with access to credit resources within a sound financial sector framework to rebuild and/or expand operations and provide for working capital (see below). In the short-run, the provision of funding under an SME Credit Program is proposed that would allow private processing enterprises access to finance for working capital and capital investment goods.¹³ In addition, the provision of technical assistance to agribusiness enterprises in the selection of new technologies, management and marketing approaches will equally be important.

36. A third critical aspect is to ensure adequate production incentives to farmers by adopting a policy aiming to increasingly target and later phasing out of donor provided food aid to the province over the coming 18 months, while acknowledging that there will continue to be food insecure segments of the population well after the summer harvest of 2000. The latter will require protection such as through public work schemes or the establishment and funding of a social safety net (pension, social welfare in rural areas).

37. Strong financial institutions that offer credit and saving services are a prerequisite for a dynamic rural sector. As there are currently no formal financial institutions operating in Kosovo and even informal systems are limited, there is an urgent need to promote the development of robust and sustainable rural financial institutions. There are a variety of models that may be followed to serve rural-based clients and the suggested approaches are not necessarily mutually exclusive. Two types of institutions are likely to be necessary. The first should be designed to serve the small scale commercial sector in rural areas, including commercial farming activities, small scale agro-processing and non-agricultural investments in rural areas. While private commercial farms comprise only a relatively small percentage of total farms, they are likely to be the ones driving future growth in the sector and producing most of the marketable surplus. Small scale processing is likely to take the lead in non-agricultural employment generation, providing an outlet for marketable farm surplus. Credit will be necessary to help commercial farms and rural entrepreneurs rebuild after the conflict, to make new investments, and for working capital.

38. A second type of financial institution will be required to serve farm and other rural households on the micro-scale end of the credit spectrum, which comprise the vast majority of households in rural Kosovo. Rural households in Kosovo are typically engaged in a variety of farm and off-farm activities. They will require small loans – for both their farm and off-farm investments – and saving facilities for small deposits, both, of which are hard for a conventional bank to provide as they necessitate very particular delivery mechanisms. Therefore, the small farm and rural household group is likely to be better served by non-bank financial intermediaries such as a rurally based microfinance institution following, for instance, saving and credit associations or credit union type approaches.

39. Immediate steps should be taken to initiate both types of institutions. There are many successful models of microfinance institutions and organizations that have a long and proven track record in microfinance development. Building on this experience, a non-bank financial institution could be initiated relatively rapidly in rural areas to serve rural clients. Agricultural and rural banks, by contrast, cannot be established as rapidly as they require more institutional

¹² The strategy for privatization of socially and state-owned agrokombinats and other enterprises is described in more detail under separate cover (see annex on Private Sector Development) in the Kosovo Reconstruction and Recovery Program.

¹³ The SME Credit Program is described in more detail under separate cover (see annex on Private Sector Development) in the Kosovo Reconstruction and Recovery Program.

development and a more elaborate regulatory framework to operate effectively. In both cases, operations should be established under an adequate regulatory and supervision framework on which UNMIK is actively working. Immediate steps are being taken to clarify the banking regulatory environment. Operational viability and lending soundness are central to the development of such financial institutions in rural areas. These requirements may, however, conflict with the possible desire on the part of the donor community (and rural clients) to channel large amounts of resources quickly into rural and agricultural sector investments.

40. **Securing rights to land and real estate properties** is a critical element of private sector development in the rural economy. This will require review, formulation and adoption of new systems and legislation pertaining to property rights, transactions, and registration to allow for the development of a secure land and real estate market that is trusted (amongst others) by credit institutions. The current state of non-registered property titles will require a province wide public investment requiring several years to formalize them, and to develop and make sustainable the necessary land registration and cadastral systems.

41. **Theme 3: Support to Institution Capacity Building.** As with the above, policies and public investments associated with capacity building and the establishment of an institutional framework for the agricultural sector would be initiated from the beginning of the year 2000, while recognizing that such endeavors require a longer development period. One element of such institution building consists in establishing the minimum agricultural administration essential to respond to the needs of the sector while limiting public involvement and employment to a few core functions covering: agricultural statistics; zoo-sanitary and key veterinary diagnostic services; quarantine facilities; food quality and safety; a simple agricultural information service drawing on mass media; and a small agricultural secretariat at the executive level (assisted in policy analysis and formulation capabilities) and with very limited representation at the municipal level. Experience suggests that it is relatively easy to expand an agricultural administration as the public takes on (and can afford) broader functions, but it is difficult to repeal an over-staffed administration at a later stage.

42. Institutional issues that need to be addressed in the medium term pertain to (a) cooperatives and associations to allow for the voluntary development of producer cooperatives and professional associations, which are important ingredients of a functional rural economy; and (b) maintenance of price and trade policies which ensure efficient markets and the free flow of internal and external trade. Technical assistance will be required to support the development of voluntary producer cooperatives and professional associations. Forest and water management will require public institutions able to protect and sustainably manage such resources. Re-establishing the higher level agricultural education and adaptive research system would equally be supported under the program.

43. In the following the program components (comprising both elements of policy and investment) previously summarized under the three themes are described in more detail.

PROGRAM COST ESTIMATES

44. Table 4 below provides an overview of cost estimates for the program described above. The suggested four-year program has tentative costs of around US\$235 million (including investment and recurrent costs) of which around US\$95 million would be incurred in 2000, US\$60 million in 2001, US\$40 million in 2003 and 2004, respectively. Around 60 percent would go to re-launching agricultural production, 25 percent to supporting private sector development in the rural economy, and some 15 percent to institution capacity building. The costs do not include project preparation expenditures which are expected to be carried by the donor community on a project-by-project basis.

**Table 4: External Financing Requirements for the Agriculture Sector
(in millions of US dollars)**

Activity	First Phase (until December 2000)			Second Phase (2001-2003)	Total
	Until March 2000	April to Dec. 2000	Total		
RELAUNCHING AGRICULTURE					
Livestock		20.0	20.0	10.0	30.0
Farm Mechanization		38.0	38.0	20.0	58.0
-- tractor and combine repairs	3	4.0	4.0	3.0	7.0
-- tractor replacements		26.0	26.0	14.0	40.0
-- farm implements		8.0	8.0	3.0	11.0
Farm Input	3	7.0	10.0	0.0	10.0
Irrigation		1.0	1.0	14.0	15.0
Rural Infrastructure (small scale)		5.0	5.0	15.0	20.0
Subtotal	6.0	71.0	74.0	59.0	133.0
PRIVATE SECTOR IN RURAL ECONOMY					
Private Veterinary Services		1.0	1.0	0.5	1.5
Agroindustries		5.5	5.5	8.0	13.5
-- agrobusiness credit facility (under SME Credit program)					10.0
-- agrobusiness TA					2.0
Rural Finance				30.0	30.0
-- rural finance company					18.0
-- rural microcredit					12.0
Land and Property Registration				15.0	15.0
Subtotal		6.5	6.5	53.5	60.0
INSTITUTION CAPACITY BUILDING					
Agricultural Administration and Public Services		4.8	4.8	12.0	16.8
-- agricultural secretariat		0.5	0.5	1.5	2.0
-- policy analysis and formulation		0.3	0.3	0.9	1.2
-- agricultural statistics		0.5	0.5	1.1	1.6
-- quarantine, diagnostic and testing	1.5	2.0	2.0	1.5	3.5
-- food quality and safety		0.5	0.5	1.5	2.0
-- agricultural information		0.5	0.5	1.5	2.0
-- agricultural higher education/research		0.5	0.5	4.0	4.5
Professional and Farmer Organizations				0.7	0.7
Forestry and Natural Resources Management				12.0	12.0
Program Management	0.5	3.5	3.5	4.0	7.5
Subtotal	2.0	8.3	8.3	28.7	37.0
Total	8.0	85.8	93.8	141.2	235.0

ANNEX II: PRIVATE SECTOR DEVELOPMENT

I. THE PRE-CONFLICT SITUATION

A. Summary of Pre-conflict Economy

1. Kosovo has a rich natural resource base, and fertile agricultural land. Over the last two decades, economic activity has centered on the extractive industries, production of raw materials and semi-finished products (lead, coal, zinc and some textiles), and agriculture. The policy and regulatory environment was based on Yugoslav-style socialism. Heavy industry was largely publicly-owned.¹ More than 60 percent of the pre-conflict population lived in rural areas, and agriculture was nearly universally privately held.

2. Despite its economic potential, Kosovo has traditionally been SFRY's poorest province. Throughout much of the 1970s-80s Kosovo received significant investment resources from SFRY's Federal Fund for Development of Less Developed Regions, largely in the capital intensive extractive industries. This support notwithstanding, Kosovo's GDP remained far behind the SFRY average due to the fact that there were few value-added activities based in the province, and to poor management of economic assets. Over the five years, Kosovo's GDP contracted by 50 percent, falling to less than \$400 per capita by 1995. In that year industry and agriculture were each responsible for about one-third of GDP, with trade and commercial activities accounting for the remainder.

3. The 50 percent decline in GDP from 1989 to 1995 was caused in large part by a dramatic drop in output levels in the industrial sector, which was comprised almost entirely of publicly-owned enterprises. Comparison figures for a few key industrial activities are as follows:

Table 1: Industrial activities in Kosovo

Product		1988	1995	% Decline
		Production	Production	
Coal	(000 tons)	11,004	7,023	36.1
Lead	(tons)	83,448	11,000	86.8
Zinc	(tons)	48,547	5,000	89.7
Fertilizer	(tons)	70,683	2,000	97.1
Cotton Yarn	(tons)	13,361	1,224	90.8
Knitted Wear	(tons)	849	260	69.3
Rubber Prod.	(tons)	10,143	1,923	81.0
Cement	(000 tons)	246	63	74.4

¹ Unless otherwise indicated, the terms "public enterprise" and "publicly-owned" are used throughout this report to mean socially-owned enterprises as well as other forms of state ownership such as enterprises wholly-owned by the state and joint stock companies majority owned by non-private shareholders.

B. The Decade of Enforced Measures (1990-1999)

4. In order to understand why the publicly-owned industrial sector contracted so badly, one needs to understand the impact of the so-called “enforced measures”, which compounded the crisis resulting from the lack of competitiveness of many enterprises, the breakup of SFRY, and the economic sanctions imposed on FRY. The program began September 3, 1990 and continued throughout the 1990s.²

- **Change of Management.** In 1990 and 1991, new management teams were appointed by FRY authorities. From this point forward, corporate management no longer rested at the local level, as had been the case under the previous self-management approach. The result was essentially to disenfranchise the largely Albanian Kosovar workforce from corporate governance.
- **Dismissals from Sensitive Posts.** From 1990 through 1991, many Albanian Kosovars were dismissed from “sensitive” posts, including management and specialist positions.
- **Lack of Investment in Spare Parts and Technology Upgrades.** Over the next decade, there was little maintenance. As a part or a machine from one of the manufacturing lines broke, another manufacturing line in the plant was cannibalized for the replacement part or machine. The result was that over time several lines became inoperative and the overall capacity of the company diminished. At the same time, there was no new investment to upgrade the technology. This hurt the competitiveness of the enterprises, particularly those engaged in higher end production.
- **Reduction of the Workforce.** Reflecting the diminished capacity of the plants, the management reduced the companies’ workforce.. As an illustration, at the textile plant in Gjilane the payroll was reduced from 2,500 workers to 1,300 over the ten-year period. Redundancies, however, affected primarily Albanian Kosovars. Over the decade approximately 140,000 Albanian Kosovars, or 10 percent of the population, lost their jobs;
- **Mergers.** In the latter part of the decade, Kosovar companies were merged into Serbian companies engaged in the same line of business. Accounts and liquid assets, including hard currency, were transferred to the new owners.

5. **Aggregate Result.** Today, the public enterprises are in varying conditions of damage and disrepair. But, there are a few general trends:

- On the **negative side**, most have had their monetary assets taken. Many have had the valuable equipment removed. To the extent that equipment remains it may be inoperative or operate at low capacity due to the cannibalism described above. The technology has not been updated, nor have the skills of the workforce.

² It is important to note that the enforced measures program applied to all public enterprises and thus affected all economic sectors. However, due to the large predominance of public enterprises in the industrial sector, its impact was hardest on production. (See the chart below listing the relative contributions of private enterprises versus public enterprises, by sector.)

- On the **positive side**, few have had their buildings damaged. Most have their land, which in some cases is quite extensive, and most still own their office space. Further, they have a labor force familiar with the company’s operations and ready to go to work (although this may not help much in the case of sectors where the technology has advanced significantly in the 1990s). Finally, due to the fact that lending to enterprises was almost non-existent in the latter period of the 1990s, enterprises have very few outstanding liabilities.

C. Contribution of the Privately-Owned Enterprises within the Formal Economy

6. Throughout the decade, the formal economy’s supporting pillar was the contribution of the private sector. This was relatively high compared to other non-Balkan, Eastern European countries and paralleled the contribution of the private sector within the rest of the SFRY, a legacy of the Marcovic era. In fact, the output levels of the privately-owned sector have remained more or less stable since 1987. As of 1996, privately-owned enterprises contributed 47 percent of the total GDP. The relative contribution for selected sectors was as follows:

Table 2: Contribution of Private Enterprises to GDP

Sector	Percent Contributed by Publicly-Owned Operations	Percent Contributed by Privately-Owned Operations
Transport and Communications	84.1	15.9
Agriculture	3.6	96.4
Construction	24.4	75.6
Trade	32.7	67.3
Industry	87.4	12.6
Total GDP	52.6	47.4

7. As of 1998, the contribution of the private sector to the overall economy had risen to 80 percent as the publicly-owned sector declined, reaching a virtual stand-still just before the conflict.

D. Development of the Parallel Economy

The “enforced measures” also led to an unintended result: the creation and promotion of a parallel economy within Kosovo. As Kosovars lost their positions at the public companies they were forced to undertake other economic activities simply to survive. Another factor promoting the parallel economy was the imposition of a series of laws that accompanied the “enforced measures” (e.g., preventing an Albanian Kosovar to register the purchase of real estate from a Serb: transfers occurred but were not recorded or Serbian straw men held title). While the official unemployment figures over the decade were significant, with some pre-war estimates running as high as 70 percent, this was ameliorated somewhat by employment in the gray market (i.e., in otherwise legal activities that were simply not part of the official system) and black market (i.e., illegal activities). Over the decade a substantial portion of the Kosovar population became expert at surviving, in some cases even thriving, outside the official economy and government structure.

II. THE CURRENT SITUATION

8. Kosovo's economy currently consists of three basic components. First, there is a large population of privately-owned enterprises. These tend to be engaged in trade and services. Second, there is a substantial parallel segment, which in the current situation where no regulatory environment is being enforced (see below) is hard to distinguish from the formerly registered private enterprises. Third, there is a finite population of publicly-owned enterprises formerly engaged in all sectors of the economy but predominately located within the industrial sector. These publicly-owned enterprises are generally in poor condition.

9. Each of these components has their characteristics and nuances, which are described in detail below. However, there are a few general points that reach across the spectrum.

10. **No Industrial Production.** Kosovo's emerging private sector does not include any significant ongoing industrial production or processing activities. As noted above, under the SFRY's policy and regulatory regime, production was limited to extracting resources. Most processing was conducted in other SRFY nations. That industry that did exist was subjected to the enforced measures. The very few private productive enterprises that existed before the war have been destroyed almost without exception. The significantly higher investment needs required to (re-)start productive enterprises would appear to hinder their (restoration) creation currently.

11. **No Banks.** There are currently no banks operating in Kosovo, nor is there a functioning payment system. While a detailed discussion of the situation in the banking sector falls outside the scope of this section, it is clear that the lack of payment and banking services contributes to the fact that private sector activity is limited to areas requiring relatively low levels of up-front investment and working capital funding. In addition, business cannot benefit from more advanced cash management or the use of alternative payment methods such as checks, or credit or debit cards. This is strictly a cash commerce system, with all of the limitations and dangers that presents.

12. There is also a significant informal banking practice that could prove dangerous. In the past travel agencies have served as conduits to move monies into and out of Kosovo. This service could easily mutate into a pyramid scheme(s) and other unregulated banking activity as experienced in other Balkan countries, undermining confidence in any nascent banking system and potentially causing a massive loss of wealth to the population.

13. **No Regulatory Framework.** In theory, the FRY's legal and regulatory regime applies today over all three components of the economy described above. With the adoption of Regulation 1, UNMIK has ostensibly borrowed wholesale the FRY's commercial law framework. In practice, none of these laws are being enforced.³

14. Therefore, with the exception of the new customs, sales and excise tax regime introduced by UNMIK on September 3, 1999,⁴ there is currently no effective regulatory framework or

³ One cannot expect this situation to continue open-ended and therefore as discussed below, in the interim, significant attention needs to be paid over whether and to what extent the FRY regime should in fact be applied.

⁴ UNMIK Regulation No. 1999/3 and Administrative Directive No. 1999/01.

registration of private business. The benefits of this extremely liberal regime are clearly reflected in the vibrancy of private sector activity described above. Unfortunately, this vibrancy is combined with worrying reports on rapidly increasing levels of criminal activity. The rapid introduction of an appropriately liberal system of business registration and regulation would be an important part of a strategy to stem this trend and move the emerging private sector into the formal economy.

A. *Privately Owned Enterprises*

15. **Retail and Services: a Vibrant Start.** The rapid return of refugees in June and July of 1999 was immediately followed by a remarkable level of activity in the private sector. New shops, restaurants, and small trading “companies” started operating literally within days of the arrival of KFOR and the rest of the large international community in Kosovo. Very quickly, these operations started to become more sophisticated, as goods started to flow into Kosovo and the owners responded to the rapidly increasing demand for services. In early September, most major towns had a vibrant retail and services sector offering a remarkably diverse supply of goods and services.

16. It is unclear whether these shops and “companies” are new, reopened enterprises formally within the official economy or restarted gray market operations (see below). And, to a certain degree the distinction is really only of historical concern. What is clear is that Kosovars clearly have an exceptional sense of entrepreneurship, as well as access to a sufficient level of investment resources to start small, capital extensive operations.

17. **Opportunities for Short-term Growth.** The success of the program of economic development and reconstruction of Kosovo depends to a large extent on the degree to which the private sector will be empowered to generate short-term growth. While the difficult political and legal issues in Kosovo are being addressed, and the transfer of the public sector into private hands takes hold, the private sector will have to step in and provide the economic opportunities Kosovars need. In addition to retail and services areas, this short-term growth is likely to come largely from agriculture, agroprocessing, construction, and the production of construction materials. Primary agriculture and construction are already overwhelmingly private, and should therefore be supported in following the lead of the rapid development of small and medium-sized enterprises (SMEs) in the retail and services sector.

B. *Parallel Sector (Gray Market)*

18. Given the nature of the parallel market, it is impossible to know its current size and characteristics. In addition, in the current situation, where there is no enforcement of any regulatory framework, there really is no clear distinction between the parallel sector and the official private economy, except a historical one. This could quickly change however as regulatory requirements are introduced. Embracing the former parallel sector as part of the official economy would be very important for the following reasons:

- First, the potential size of the parallel segment is huge. While not all Albanian Kosovars were employed by the public enterprises (and thus were not affected through the loss of their job), all were affected by the post-1989 legal regime. To some degree, all Albanian Kosovars have led some portion of their daily lives within the parallel economy. Thus, they have at least some expertise that could help them remain outside of the official economy if they so choose.

- Second, the predominant gray market activity of in the parallel economy is in the trade and services areas, on a small to medium scale – a sector likely to grow substantially in the near-term.
- Third, the activity within the parallel economy could contribute to the tax base (since it enjoys the benefit of governmental services provided to the general population). The gray market was subject to the parallel government established by the Albanian Kosovars and funded through informal domestic taxes and the voluntary tax on Albanian expatriates.

19. It is unclear to what extent persons within the parallel economy will welcome the chance to participate in the organized economy. While one might expect that Kosovars who were previously excluded would welcome the chance to live and work within the recognized system, that enthusiasm may fade as persons realize it comes with a cost in the form of taxes. However, the parallel economy could provide a tremendous boost to the official economy if it sheds its gray status, with the growth push most likely occurring in the trade and services sectors. This is not likely to occur, however, without adoption of policies designed to embrace this sector and/or to force it into the official system.

C. *Public Enterprises*

20. **Ownership.** There are currently around 200 public enterprises in Kosovo, out of which 66 could be classified as major enterprises. These numbers include both industrial enterprises (including agro-industry) and public utilities. Although all of these enterprises were under so-called “social ownership” prior to 1989, the current ownership situation is less than clear. In many cases the enforced measures have resulted in competing claims between the former workforce -- claiming that “social ownership” equaled “ownership by the workers” --, and various claimants to ownership, either in the form of shareholding, or through complete integration of the Kosovar enterprise into a Serbian one (as was the case for Jugobanka). In some cases, the situation is further complicated by commercial contracts or concession arrangements with foreign companies. Generally speaking, the larger the enterprise is the higher the degree of complexity in the ownership situation. Medium sized companies such as brick factories and slaughter houses are essentially local ventures, while at the opposite end of the spectrum, the huge Treпча mining complex represents a very complex case in the study of ownership issues.

21. **Viability.** Virtually all enterprises suffered heavy damage as a result of neglect and lack of maintenance throughout the 1990s, leaving them in a generally dilapidated physical state, often not much more than non-operative outdated production lines, some buildings and land. Most enterprises would need significant re-start capital to be able to produce at any level at all. In addition to the physical damage, however, the enterprises suffer from a far more serious problem in having lost the markets they used to serve, as the rest of the Balkan region has moved on from 1989 and FRY no longer presents a viable market for most of the products previously manufactured in Kosovo. Finally, the management and workers at most enterprises have not worked for ten years, which leaves their skills severely out of date, having missed both the first ten years of transition and the technological revolution of the 1990s.

22. **Political Perceptions.** The situation described above creates a huge political and social problem in Kosovar society. Enterprise workers, having been dismissed from their jobs in the early 1990s and having been forced to take care of themselves in the parallel system, have returned to their enterprises only to find them destroyed. The immediate psychological reaction to this “discovery” is a strong desire to bring the enterprises back to their state during the “golden age” before 1989. In discussions with Kosovars on these issues, there is a very strong sense of

entitlement to compensation, and an almost complete denial of the fact that many of these enterprises would not have been viable even if they were in the best possible physical shape. This is likely to translate into strong pressure for subsidies to public enterprises. The situation in this regard appears potentially worse than was the case in other transition economies at the start of the transition process. It will be very important to manage the resulting expectations carefully through a process of intensive dialogue with leading thinkers on enterprise issues in Kosovar society, and through public education.

23. **Social Problems.** On the other hand, the social problems associated with the restart of these enterprises are somewhat less pressing than is typically the case in a transition economy. Although most workers have actually not worked in these enterprises for ten years, they have successfully managed to take care of themselves, largely in the private sector or parallel economy, and through remittances from family members abroad. It would therefore be false to assume that large social problems would be created if enterprises were not to start up soon. The distinction from the experience in other Balkan countries is very important, since it essentially means that if appropriate policies are implemented, there will be fewer problems associated with vested interests in dealing with enterprise issues. There also is a high premium on honesty in the debate about viability of these enterprises, as many of the workers might be better off remaining in their activities of the last ten years and becoming part of the genuine private sector.

Larger Enterprises: Little Short-term Potential

24. As a result of the problems described above, the large enterprises need investment, modern management, and access to new markets to have any chance of being viable. For most of these enterprises, which depend on exports for their markets, and need sophisticated and expensive capital goods, attracting foreign investors will be crucial for restarting activities. The lack of clarity in Kosovo's legal framework and the issues related to ownership explained above will make it practically impossible to achieve this quickly. It is therefore unrealistic to assume that large public enterprises in Kosovo will make a significant contribution to economic growth in the short term.

Smaller Public Enterprises: Good Opportunities for the Domestic Market

25. As discussed above, there will be strong potential for growth in provision of services (especially to the very large international community present in Kosovo), agriculture and agroprocessing, and construction. While the service and construction sectors are already overwhelmingly private, the same is not the case for agroprocessing and the production of construction materials. Most enterprises in these two sub-sectors seem to be in only a somewhat better physical state than the large enterprises. However, they are simple operations of relatively modest size. Therefore, they will be much cheaper to re-start based on domestic resources, both in terms of investment and management. Typical amounts needed to restart the construction material factories, as cited by the managers, range from US\$160,000 with few exceeding US\$500,000. In addition, these enterprises are essentially local operations, with a much lower degree of complexity in their ownership situation.

III. STRATEGY FOR PRIVATE SECTOR DEVELOPMENT

26. In light of all of the above, growth in the enterprise sector in Kosovo will be driven almost completely by privately-owned small and medium-sized enterprises (SMEs), old and new. The strategy for private sector development should first promote the growth and development of the privately-owned enterprises already within the official economy. Second, it should embrace

the parallel economy and bring it within the official economy through a combination of inducement and requirement. And third, it should transfer the potentially viable public enterprises to private ownership while freeing up the assets of non-viable enterprises through liquidation.

27. The most promising sectors in the short term are likely to be privately-owned trade and services, which, as noted above, have already demonstrated a remarkable rebound. Closely following these sub-sectors should be privately-owned agricultural production (assuming the effective assistance of donors), and newly-privatized agroprocessing and construction. Allowing the existing private sector to lead the way, shortly followed by the newly privatized sub-sectors is likely to have a high short-term pay-off. This would create the breathing space necessary to work on structural solutions for other sectors of industry and mining, which will need considerable time to adjust to the dramatically changed circumstances around Kosovo in the year 2000 and beyond.

28. Policy developments need to be accompanied by a comprehensive consensus building campaign and, once the policies are set, a substantial public education program. The consensus building should be aimed at ensuring that the Kosovars are partners in developing what one day will be their government. The public education effort should be aimed at the general public in order to bring their expectations levels in line with the current reality and to convey the salient points of the new structure of the economy. The specifics of each work area are discussed immediately below.

A. *Setting the Legal and Regulatory Framework for Private Sector Development*

29. In order to support private sector development, UNMIK needs support in the formulation and introduction of a regulatory environment that results in costs of operating legally significantly less than the cost of operating illegally. This is essential to embracing the parallel economy. In addition the legal regime needs to provide for and promote the availability of credit by protecting private property rights and allowing for the practice of collateral for lending. Further, the regime needs to be flexible enough to allow for financing vehicles such as venture capital funds for private productive activity.

30. However, the current regulatory framework in Kosovo is unclear. This creates a situation of great uncertainty to which there is only one logical response for the emerging private sector: *stay underground*. As this creates a perfect breeding ground for organized crime to step into the vacuum left by the authorities, there is a very high premium indeed on introducing a clear and simple legal framework.

31. In broad terms the successful framework should have the following characteristics. It should: (i) be simple, understandable and enforceable; (ii) allow for easy compliance; (iii) allow as little discretionary authority as possible to minimize the scope for corruption; and (iv) eliminate duplication with existing FRY regulations. The framework should include the following elements:

- An effective and simple business registration system;
- An appropriate property rights legal framework, including collateral and bankruptcy legislation;
- Basic business law and contractual rights legal framework supportive of private business formation and operation;

- A practical legal mechanism for resolving property disputes;
- A competition law framework which severely limits the scope for public intervention in industries which are not natural monopolies;
- A comprehensive accounting legal and regulatory framework which promotes the application of International Accounting Standards for financial and tax accounting purposes.

32. As it will take considerable time to complete this framework, and even longer to create the institutional capacity to implement it, it will be crucial to prioritize work according to a critical path analysis which focuses on removing the biggest obstacles first.

33. **Links with the Trade Regime.** As the recently introduced trade and taxation regime is refined, careful attention should be paid to the cumulative effect of the various fees and taxes on private business. Currently, customs fees, sales and excise taxes are being charged only at half the border of Kosovo. As taxation inside Kosovo is introduced, careful attention should be paid to the overall tax burden on enterprises, especially in light of the high sales taxes levied at the border. In addition, the trade regime will need to be refined in order to avoid taxation, which will unduly hurt the prospects for private sector-led growth in Kosovo. For example, a rebate system needs to be introduced in the medium term to stimulate processing, sub-contracting and consignment deals which will be important to allow Kosovo to exploit its abundance of labor, also, it may not be in the interest of Kosovo's economic development to tax imported capital goods, even in the short term.

B. Credit for Private Enterprises

34. The absence of a banking system that can provide credit for viable productive activity is probably the most serious constraint to private sector growth in Kosovo. As a consequence, the private sector is limited to activities that require minimal investment, mainly in the services and retail sectors. Filling this void with a credit program based on sound economic and financial principles is therefore very important.

35. **SME Credit Program.** UNMIK intends to formulate the basic principles and values which would form the basis for an SME Credit Program for Kosovo, including:

- SME lending activities must be conducted within the newly established banking supervisory regime;
- Credit should be extended through the Program for private enterprises only, based on sound credit analysis;
- Credit should be extended to enterprises in the parallel sector only upon their conversion to the official economy (i.e., that they register as enterprises and fully comply with the legal regime)
- Borrowing terms extended to enterprises should not distort competition with commercial credit as and when this develops;
- In addition to "urban" SMEs, the Program should also cater effectively for lending to agroprocessing enterprises;

- The Program should be conducted in such a manner that supports the medium term institution building needs for the banking sector;
- Donor financed SME credit should be viewed only as a transitional mechanism until a healthy banking system will be developed; and
- Donor coordination must be maximized and overseen by UNMIK itself;
- Apply similar principles to the extension of micro-credit and agricultural credit.

36. Grants to enterprises without any form of financial intermediation are currently being considered and/or implemented by a number of donors, in view of the absence of formal credit. Anecdotal evidence suggests that these programs are not coordinated and, for example, that some enterprises may receive support from various donors. UNMIK is expected to tackle this problem by setting up a donor coordination forum for the enterprise sector. However, such grants can also create serious distortions. They are likely to strengthen resistance to structural changes and reforms, notably privatization, and to entrench resistance to a forward looking development strategy. In those exceptional cases where donors might provide grants, they should be strictly limited in scale and focused on urgent requirements in sectors where an economically viable supply response can be expected (for example, in construction). This should be discontinued as soon as SME credit programs, on which donor effort should be concentrated, provide an alternative.

Other Support for Private Enterprises

37. There are several other useful interventions to be considered in support of SME development, most of which have been implemented in other transition economies:

- **Business advisory services** can introduce the business community to skills like the development of a sound business plan and credit application and accounting and auditing, making important contributions to capacity building in the sector. Programs providing these services could be quite useful, as long as the use of the program would be optional, and certainly not a pre-requisite for access to SME credit, as experience shows that this would create potential for collusion and corruption; and
- **Venture capital funds** can increase the amount of resources available for equity investment into Kosovar businesses. These programs could be very useful in channeling diaspora capital to legitimate investment in Kosovo.

C. Converting Public Enterprises to Private Ownership

38. Transforming existing public enterprises into economically viable firms that contribute to growth and employment is a major challenge. To this end, UNMIK intends to formulate and implement a policy aimed at transferring the ownership of the publicly-owned enterprises into private hands. Experience in other transition economies suggests that private sector involvement will increase investment flows, which are urgently required in Kosovo for reconstruction and economic recovery. Private ownership can also be expected to maximize the incentive for improving management and making economically viable investment. Finally, private ownership will reduce pressures for subsidizing public enterprises – which are unlikely to have a lasting effect on the productivity of the enterprises, and which are a burden on scarce public sector budget resources.

C.1. Generating short-term growth through selected sales of agroprocessing and construction materials enterprises.

39. UNMIK intends to pursue a strategy aimed at allowing the private sector to invest in those assets in the public enterprise sector which have strong potential to contribute to growth in the near-term, while setting the stage for dealing successfully with the major enterprises in due course. Such a strategy would focus first on implementing a program of selective sales that would bring the assets in the agroprocessing and construction materials into private hands so as to allow these sectors to develop rapidly in response to strong domestic demand during the reconstruction phase. Most enterprises in these two sub-sectors, around 35 in agroprocessing and about 20 in construction materials, are essentially local operations that were not integrated with Serbian enterprises. Local communities are consistently listing the re-start of these enterprises -- typically the local brick factory or the dairy plant -- as their highest priority. There could therefore be very strong political and social momentum behind a well-designed program to get these enterprises back to work, this time in the private sector. The strong demand for both agroprocessing capacity and construction materials expected next spring in association with the restart of agricultural activity and the rebuilding effort could add to this momentum.

40. Program design. The program of selected sales would be designed to maximize the chance of achieving the main objective: to contribute to growth by Spring 2000. This means that the design will have to maximize the scope for attracting investment and improving management, and to allow for rapid implementation, within the next six months. The option envisaged is to transfer ownership of the enterprises through local tender. This method is easy and quick to implement. If combined with pre-qualification of bidders on criteria aimed at establishing their genuine ability to invest in and manage the enterprise in question, it will also achieve the other objectives set out above. As the objective of this program would not be to raise revenues but to transfer assets into private hands and maximize the injection of capital into the enterprise, it would be preferable to select the winning investor based on the amount (s)he is prepared to invest. Although one would expect the vast majority of investors in these enterprises to be domestic, there would be no reason for excluding foreigners from participating in these tenders. The sometimes suggested alternative to transfer ownership wholly to the workers cannot be expected to allow the enterprises to attract the amount of investment required to ensure viability and create jobs, nor is it likely to improve management. It should therefore be rejected, as it already is by many leading thinkers on enterprise issues in Kosovar society

41. **Workers' rights.** While there is general acceptance that giving the enterprise to the workers is not a good option, there is a legitimate concern that workers have rights to at least part of the enterprise in which they are employed. This was the case in virtually every transition economy so that there is ample precedent for addressing this issue. Essentially the approach would be to give workers a share of the enterprise which would be sufficiently large to be meaningful if the enterprise did well, while preserving fully the possibility of the management to take the necessary decisions to ensure the economic viability of the enterprises. This would typically be achieved by giving the workers a 15-20 percent share in the enterprise.

42. In cases where it would be difficult or controversial to establish who would be entitled to this share, there would be no reason to delay transformation of ownership. It would be sufficient to reserve a 15-20 percent stock option to the collective of workers, which could be converted into actual shares when a final determination was made on who would be entitled to these shares. The advantage of this approach is that the enterprise can be brought into private hands without having to await the outcome of the potentially lengthy decision-making process on workers' entitlements.

C.2. Privatizing Large Public Enterprises

43. Since the ownership situation of most of the large enterprises is complex, this group cannot be dealt with without first establishing how UNMIK intends to deal with the various competing claims, and putting in place an arbitration mechanism to sort out individual claims. This work, which would likely result in an UNMIK regulation on public ownership, should be based both on legal research and an extensive political dialogue, probably involving both the Legal Advisory Council and the Economic Policy Board. Without prejudice to the outcome of this process, it is important to point out that the adopted approach should be viewed as credible in Kosovar society and should not violate international law. A number of leading thinkers in Kosovar society have already done considerable work on these issues, which is generally characterized by its realism and pragmatism.

44. UNMIK intends to set up an ownership and privatization working group under the auspices of the Economic Policy Board. This group could provide important input into the work on public ownership described directly above and start focusing relatively quickly on the design of a program for privatization of large enterprises. Current thinking in Kosovo is that such a program should be implemented only after elections, however, there would be a very high premium on trying to reach a consensus and on creating the legal basis for a pilot program to take place in the year 2000.

Public debate and a public education program. In addition, it is of paramount importance to start a public debate and a public education program on large enterprise privatization as early as possible. The main purpose of this debate and education program would be to get the message across that Kosovo's economic future does not lie in recreating the Kosovo of 1989, but in building a different Kosovo based on current and future economic realities and opportunities. At the same time, it will contribute to deal with the unrealistic expectations that both the workers and the general population may have about the viability of large enterprises in Kosovo.

A pilot program for large enterprise privatization. The purpose of a such program would be to strengthen the consensus on the overall approach by setting a positive example. This would have the additional benefit of bringing some of Kosovo's best large enterprises into private hands as early as possible, so that they can start contributing to growth. Since these enterprises will need foreign strategic investment, the basic method for this program would be privatization through tenders to strategic investors, with similar provisions for workers' rights as discussed in the section on agroprocessing and construction materials enterprises above. To maximize the chance for success, the financial advisers who would assist in the implementation of this pilot program would receive an incentive-based reward.

After the pilot. If the pilot program is successful, it might be possible to follow with another "batch" of enterprises under a similar program, possibly allowing for adjustments in the program based on the experience with the pilot program. If it appears that some enterprises are not attractive enough it will be important to switch gears to a solution that is aimed at disposing of the remaining assets as quickly and efficiently as possible while avoiding any solution which will call for public subsidization.

D. The Climate for Foreign Investment

45. **Foreign Investment Law.** The strategy for large enterprises outlined above cannot be implemented without a sound framework for foreign investment into Kosovo. UNMIK should therefore start work on the preparation and adoption of a foreign investment law as soon as

possible. This law should enshrine the basic principles of any sound foreign investment climate: protection of investors' rights, non-discriminatory treatment for foreigners and locals, and access to fair arbitration. There are plenty of examples of laws that meet these criteria, which could be adopted without significant revision.

46. **Political Risk Insurance.** Due to the specific legal and political situation in Kosovo, even a perfect foreign investment law would not suffice to bring in the amounts of investment that are likely to be needed to make at least a number of large enterprises a success. Any investor would have to be protected against the risks posed by the uncertainty over Kosovo's eventual status. This should be addressed by ensuring the availability of effective political risk insurance for investment, if at all possible in cooperation between donor agencies and the private insurance market following the recent Bosnia precedent. This approach would limit the amount of donor funds required, and it would introduce the private market to Kosovo, thus ensuring a larger degree of sustainability.

IV. PROPOSED DONOR INTERVENTION

As the private sector development program begins there are three tasks confronting UNMIK and the donor community. First, UNMIK needs technical assistance for the formulation of its policies relating to the legal framework, SME lending and the privatization process. Second, implementation needs to begin, with funding from the donor community flowing to the key areas in need of support: SME lending and implementation of the privatization process, including the provision of effective political risk insurance. Third, there needs to be strong donor coordination as the projects unfold, to be achieved by a combination of UNMIK oversight and donor cooperation. The necessary donor interventions, and the associated costs, are summarized in the table below:

Activity	First Phase (until December 2000)			Second Phase (2001-2003)	Total
	Until March 2000	April to Dec. 2000	Total		
INVESTMENTS					
SME lines of credit	0.0	30.0	30.0	20.0	50.0
Credit Lines through the banking system.	0.0	0.0	0.0	35.0	35.0
Business advisory services	3.0	12.0	15.0	10.0	25.0
Venture capital funds	0.0	20.0	20.0	15.0	35.0
Reconstruction Support Program.	0.0	10.0	10.0	5.0	15.0
Political risk insurance for foreign investment.	0.0	25.0	25.0	20.0	45.0
Subtotal	0.0	97.0	100.0	105.0	205.0
TECHNICAL ASSISTANCE	13.3	6.7	20.0	5.0	25.0
Total	16.3	103.7	120.0	110.0	230.0

47. Technical expertise, within UNMIK or provided through technical assistance, will be particularly needed in the short-term in the following areas:

- (i) Establishing the legal framework for private sector development (attorney(s) to draft an enterprise law, property rights framework, commercial code, bankruptcy law, competition law, and accounting law framework);
- (ii) Preparation of the privatization program (specialists to develop an enterprise privatization strategy and oversee its implementation); implementation and design of the privatization strategy will need to be supported by an extensive public debate and information campaign, for which technical assistance will be necessary.
- (iii) Development of SME Lending Strategy. While it is UNMIK's responsibility to develop its policies towards SME lending, again the actual strategy should be created in consultation with the donor who will form the lending mechanisms and conduct the actual programs.
- (iv) Privatization Support Program. As a preface to commencing actual privatization auctions, an assessment of technical support for privatization is needed. In order to maximize success of the auction(s), a package of technical support, market-based, donor-provided lending and purchaser investment requirements must be created and announced at the time the companies are tendered.
- (v) Perform Privatization of Agroprocessing and Construction Materials Enterprises. Under the strategy laid out above, privatization of the agroprocessing and construction materials businesses is scheduled for "fast track" privatization. The donor community needs to provide the actual manpower to perform this task.
- (vi) Start Preparation of Privatization Program for Large Enterprises. Following on the overall privatization strategy to be created as described above, technical assistance will be required to design the program and execute the pilot program for the first 10 enterprises.

ANNEX III: HOUSING

A. HOUSING SECTOR DESCRIPTION

Description of the Housing Sector before 1989

1. The evolution of the housing sector in Kosovo between 1945 and 1989 reflected changes in the prevailing political and economical situation in the Socialist Federal Republic of Yugoslavia. In the period immediately after World War II, the economy was in very poor state, and there was serious deterioration in the physical condition of the urban centers in particular. Housing in the rural areas remained of poor quality due to the predominance of subsistence agriculture, supplemented only by some poorly paid employment in the manufacturing industry. Subsequent intensive exploitation of mineral resources from the 1950s onwards brought some improvements. The 1970s witnessed the steadiest growth period throughout the Social Federal Republic of Yugoslavia, including Kosovo; this was accompanied by increased housing construction in the larger urban centers. A major recession in the 1980s, with a crisis at the end of the decade, led to a major downturn in the housing sector, particularly after 1989.

2. While access to statistics is difficult at this time, figures available for 1985 indicate that from a working age population numbering 950,000 (54 percent of total population of 1.76 million), only 210,000 or 22 percent were in salaried employment, with 10 percent of this employed group (22,000) being engaged in construction. The concentration of construction workers was greater in Prishtine and the larger towns than in the rural areas. In the major urban centers, large state-owned construction enterprises built high-rise flats as collective housing on behalf of state enterprises in all sectors, which wanted to provide housing for use by their employees. In the towns and rural areas, craftspeople and small unregistered private firms undertook low-tech construction of individual houses. In the 1970s and 1980s, annual construction outputs of urban flats (state-owned) and private houses were on the order of 1,000 and 6,000 units respectively, indicating the significantly higher capacity of the growing private housing contractor sector.

Recent History of Housing Sector (1989 – 1999)

3. Since 1989, Kosovo's economy, including the housing sector, deteriorated rapidly. Following the political changes in the SFRY in the late 1980s, and the attendant series of conflicts, most of the state-owned construction firms were devastated. Kosovar Albanian employees in particular were made redundant, and much of the construction equipment was removed. From 1990-1997, almost 500 private construction firms were registered in Kosovo, though only 40 percent of these were active, mostly in construction of housing and small commercial units. It is estimated that a further 500 unregistered small construction teams were also in existence.

4. Counterbalancing to some extent the decline in the economy, significant remittances from the Kosovar Diaspora in Switzerland, Germany and elsewhere during the 1990s are reported to have funded much of whatever housing construction took place. Overall, 80 percent of recent private sector investment in Kosovo has been assessed to have been in housing. During the mid-1990s, it became possible for most occupants of collective housing flats to buy out ownership from the state enterprises for very low payments.

5. The officially recorded output of *completed* housing units dropped in the 1990s to approximately 25 percent of the levels of the 1980s, with records indicating only 168 flats and 1231 private houses being completed throughout Kosovo in 1995. However, these statistics do not take account of ongoing construction work on the very significant number of partly finished dwellings seen throughout the province, many of which were started in the late 1980s and have proceeded at a slow pace in the 1990s. Meanwhile, during the 1990s, some private firms began to manufacture prefabricated construction products for use in housing and commercial construction.

6. Housing construction took a further rapid decline following conflict in 1998. Among the few activities of contractors was their successful involvement (on behalf of aid agencies) in the winter of 1998 in making emergency shelter repairs to damaged houses. During the recent conflict from March-June 1999, destruction and looting of facilities and equipment led to additional setbacks to the capacity of building product manufacturers and construction firms, with both the small private firms and the larger former state firms being seriously affected.

Current Situation in Housing Sector (since June 1999)

7. Many small housing construction firms have started up again, and have become engaged in rehabilitation work on behalf of the owners of damaged houses and small urban commercial units-- in addition to construction works for humanitarian agencies and KFOR military facilities. Meanwhile, the skills of many individual craftspeople are being utilized through their direct employment by humanitarian agencies engaged in shelter and rehabilitation programs. Other craftspeople are applying their skills in support of their own local communities. However, there are indications of a shortage of sufficient skilled workers to support the extent of forthcoming reconstruction works.

8. Those building product firms that still have sufficient functioning equipment are getting back into production, while materials for reconstruction efforts are being supplemented by very significant supplies of timber and other building materials being imported from neighboring countries in the Balkans and beyond.

9. Quite apart from the implementation capacities of construction firms, NGOs, KFOR and craftspeople, a major strength to be harnessed at this time in Kosovo is the motivation and sense of initiative of Kosovars to help themselves-- whether it be for housing rehabilitation or in availing of any economic opportunities to empower themselves. Since June 1999, one of the largest and fastest spontaneous returns of refugees in the world has been witnessed in Kosovo. Many Kosovars have also undertaken to restore their houses-- without substantial external assistance. It is now important that communities themselves be meaningfully involved in determining how best to proceed.

Extent of Damage to Housing

10. Damage to dwellings and public buildings in Kosovo began on a significant scale as early as October 1998, though of course the extent of the damage escalated enormously during the recent conflict from March 24, 1999 - June 12, 1999. Upon the withdrawal of the FRY army from the province of Kosovo, the International Management Group (IMG) undertook a quick damage assessment throughout Kosovo which was completed in time for the donors' conference on July 28, 1999 in Brussels. The assessment provided a detailed picture of the damage done to the housing in Kosovo, awarded damage category levels to each affected house, and included preliminary cost estimates for the damage caused. This-EC funded assessment complemented other assessments for damage to housing as undertaken by the US National Imagery and Mapping

Agency (NIMA) and by UNHCR, and was assisted by inputs from KFOR military brigades and NGOs.

11. It is estimated that 120,000 houses out of a total Kosovo housing stock of approximately 250,000 have been affected by damage or destruction (see Table below), mostly due to being set on fire but also resulting from artillery and gunfire. The population affected by having homes in the two worst IMG damage categories (III and IV), and therefore potentially the most vulnerable to the extreme weather conditions in the oncoming winter months, is estimated to be over 500,000. Tentative cost estimates for the total rehabilitation of a 75 square meter area for each affected household amount to US\$1,060 million.

Table 1: IMG Damage Assessment in the Housing Sector

Damage Category	I	II	III	IV
Level of Damage	5 – 20 percent	20 – 40 percent	40 – 60 percent	Over 60 percent
Description	Slightly damaged	Heavily damaged	Uninhabitable	Beyond cost-effective repairs
Approx. number of affected units	23,000	18,000	32,000	47,000
Percentage of total housing stock affected	11 percent	9 percent	16 percent	23 percent
Average total rehabilitation cost for a 75 sq.m. area (in US\$)	2,170	5,000	7,830	14,150
Total rehabilitation cost (in US\$ million)	50	90	250	665

B. PRIORITIES FOR RECOVERY OF HOUSING SECTOR

Objective

12. The overall objective of the sectoral recovery program must be to ensure that sufficient housing of reasonable standard is available in the right locations to satisfy the needs of the population of Kosovo-- whether the housing is provided through donor-assisted rehabilitation programs or through new construction / rehabilitation funded by dwelling owners themselves.

13. This will require activities in three subsectors:

- Rehabilitation of the largely destroyed private housing stock. Since assistance and implementation capacity are limited, there will be a need to ration and target support. But every effort should be concentrated in the coming year to ensure that the major part of planned donor-assisted rehabilitation of dwellings is completed within 2000.¹

¹ In advance of the coming winter some agencies have chosen to weatherproof a number of almost completed new houses, viewing this as a more rapid means of providing immediate shelter for groups of families than repairing seriously damaged houses. It is unlikely that support to such houses would continue in spring 2000.

- Improvement of collective housing. This will mainly require regulatory action, in particular, to clarify ownership and maintenance arrangements. Although less pressing, needs are important, and should be addressed as soon as possible.
- Restart of the construction industry is described in a separate annex. The private contractor and building product sectors will need support to satisfy the needs of all construction efforts, whether rehabilitation or new building requirements, and whether funded privately or by donors. Catching up on the deficit of normal housing expansion that did not take place in the last ten years will place additional demands on the private construction sector.

14. The strategy for assistance to the housing sector must also take into full consideration the wider context of related aid to rehabilitation of public facilities (e.g. schools, health centers), utilities and infrastructure, community building initiatives, and support to livelihoods through job creation and income-generating projects, etc. Aid put into fostering rural and urban livelihood opportunities will complement housing rehabilitation initiatives, as Kosovars will have income sources to continue to self-finance rehabilitation work. Municipal investment funds for local utilities and other infrastructure works will provide complementary support to housing construction.

15. Many returning refugees and IDPs are gravitating toward Prishtine and other urban centers. While this migration may be attributed in part to the greater extent of destruction of dwellings in rural areas, especially in the more remote parts, the attraction of the urban centers is also based on expectations of income earning opportunities and improved access to public and other services in urban areas. Now that many people have made a break with their home villages many will never return, whether it be for economic, security or other reasons. Such a trend of migration from rural areas to larger urban centers would not be a phenomenon unique to Kosovo. However, it should be noted that older Kosovars in rural areas may maintain a family presence even if many younger people opt for the city life. It is important to ensure that rehabilitation assistance is only provided where there is certainty as to future permanent occupancy of the dwellings. Implications of the urbanization scenario are that: (i) not all damaged houses in rural areas may need to be rehabilitated given the absence of permanent owner occupiers; and (ii) new housing, in addition to rehabilitation of existing units, will be required in urban areas.

Rehabilitating Damaged Housing

Targeting of Beneficiary Households

16. In view of the extent of the damage, and of the limited implementation capacity, external assistance will have to be rationed and targeted. Consistency among donors on rationing and targeting mechanisms will be key to ensuring fairness, effectiveness, and transparency. Minimum and maximum rehabilitation standards, as well as targeting criteria, should be defined under UNMIK's auspices. The agreed criteria and guidelines should be broadly publicized, as early as possible, to avoid any potential deterrent to better-off home-owners to start self-financed rehabilitation works based on false expectations of eligibility for aid.

17. **Rehabilitation Standards.** In view of the limited funding available, there will be a trade-off between the number of housing units repaired and the level of rehabilitation undertaken. An equitable upper limit of assistance that can be given to targeted households is tentatively defined in terms of materials sufficient for a reduced floor area of 75m², at standards consistent

with those published by IMG, leaving the cost of any additional floor area extension to the responsibility of the owner.²

18. **Targeting of Beneficiary Households.** To date, immediate shelter assistance has been primarily directed to those units which were relatively less damaged, could be fixed before the winter, and could potentially accommodate a number of families. In the coming phase, assistance for permanent rehabilitation should be allocated based on the vulnerability of the beneficiaries, in addition to the condition of the house.³ Families in up to 60 percent of the houses in IMG damage categories II, III, and IV (which corresponds to approximately 60,000 households) should be eligible for vulnerability-based assistance (this figure is obviously subject to adjustment with the restart of economic activity throughout 2000):

- The 20,000 most vulnerable households (who cannot carry out significant repairs by themselves) would be eligible for financial assistance corresponding to rehabilitation (materials and labor) for a 75 square meter habitable space; and
- Another 40,000 households should receive assistance in the form of materials only for “primary rehabilitation” of on average 75m² of habitable floor space.

As a starting point, beneficiaries could be identified with assistance from Kosovo’s Mother Theresa Society. Lists should be adjusted under UNMIK’s guidance to take into account additional information available.

19. After the winter, or during it where possible, the first priority for rehabilitation assistance should be those households satisfying the targeting criteria, and those which are either sharing the accommodation of others (normally because their own houses are in even worse condition and incapable of benefiting from shelter repair kits) or accommodated in collective centers. With regard to the latter, UNHCR estimates that up to 20,000 places will be made available in collective centers (mostly in allocated public buildings) for people who may have to resort to this form of shelter over the winter. There will also be a need for close monitoring of the pressures caused by urbanization of the population over the winter, with programs responding to needs presented.

Donor Coordination on Coverage of Housing Assistance Programs

20. The geographic targeting of municipalities and villages for future funding of housing rehabilitation must take fully into account not only relative differences in damage levels, but also the combined extent of current assistance coverage by both KFOR and NGOs in each area, as there can be significant variations between areas. UNMIK, local government, UN agencies and donors will need to continue to coordinate the division of housing-related responsibilities to

² In the case of a large house where two or more targeted households occupy one floor each, then rehabilitation costs for a multiple of 75m² floor area could be eligible for funding. For the case of destroyed buildings in urban centers which had included a ground floor commercial unit and housing accommodation on the upper floors, the same guideline would apply in that reconstruction of 75m² of floor area per household could be funded. Any potential funding for the commercial unit component would need to be treated separately.

³ There will also be a need for coordination and consistency in targeting of assistance in the complementary areas of housing, agricultural and social welfare supports.

organizations by geographical area, while maintaining flexibility to respond to emerging needs in the more vulnerable areas.

21. It is recommended to establish, under UNMIK's auspices, and with extensive engagement of Kosovar experts, a small unit for coordination of the housing program, which would in particular: (i) set guiding principles on targeting, as well as on rehabilitation standards, to ensure an adequate, fair and transparent process of beneficiary selection, making allowance for local introduction of regional specifics; (ii) coordinate donor activities in the sector, through a formal registration requirement for all donor-funded programs, disseminate information, and advise donors to ensure an adequate geographic coverage of Kosovo; and (iii) regularly revise and adjust target rehabilitation standards, and evaluate their implementation.

Implementation

22. A number of alternative approaches may be taken to implement the rehabilitation programs – and it is not intended to prescribe any single mechanism, though common standards of achievement are recommended. The task is so large that it will be necessary to mobilize all actors that have capacity, including beneficiary communities themselves, local craftspeople, private contractors, NGOs, UN agencies and municipal authorities. The relative success of different approaches will be evaluated from late 1999 through summer 2000.

23. The involvement and capacity building of municipal government structures, led by UNMIK or otherwise, must be central to the implementation of housing sector programs. Municipal authority housing commissions can play an important role in: (i) prioritization of villages; (ii) receipt of individual applications for assistance from households; (iii) verification of house ownership; (iv) compliance with planning and other regulations; (v) environmental considerations; (vi) technical assessment of rehabilitation needs; (vii) adjudication on applications (e.g., by scoring against targeting criteria); (viii) monitoring of progress and quality of construction work; and (ix) coordination of information on the provision of assistance in the municipality. In addition to the municipal level, village level committees also need to be engaged in the transparent application of targeting criteria for selection of beneficiary households.

24. As a general principle, efforts should be made to leverage Kosovar resources, through the use of 'self-help' projects, with communities encouraged to provide labor assistance to their less able and vulnerable households. Wherever possible, donor support should be limited to the provision of basic building materials, and possibly funding of skilled labor (e.g., for carpentry, water or electric power). Local procurement should be encouraged. Some works may need to be financed, including for the most vulnerable, or where adequate craft skills are not freely available to ensure quality workmanship. Implementation could be managed by an NGO increasingly working in partnership with revitalized municipal authorities, or indeed with the latter party only.

25. Materials may be directly handed over to beneficiary households based on the results of individual house assessments. A voucher system would be preferable. Beneficiary households could be given vouchers (value corresponding to the assessed damage category) to be exchanged for construction materials at nominated supply locations, whether these be private traders' premises, or warehouses managed by municipal authorities or NGOs. Consideration can be given to mechanisms for permitting households to transfer the use of the voucher materials to an alternative housing location in Kosovo, if the beneficiary household has already moved or intends to do so. The emphasis is on flexibility and maximum control by the beneficiaries.

26. While self-help is the more ideal situation, rehabilitation undertaken directly by private contractors has the advantages of greater certainty that the work will be done. It is also easier to verify the correct use of materials, ensure better quality workmanship, thereby contributing to recovery of the construction industry sector, and support of the local economy through employment. It is recommended that this option be considered for rehabilitation of the most damaged homes, as well as those of the most vulnerable groups, which may need assistance with the provision of paid skilled labor.

27. To supplement grant type assistance for those households targeted as being the most needy, the introduction of credit schemes will be necessary to facilitate the general population to make private investments in reconstruction of housing, thus providing an extra impetus to the market.

Box 1: KFOR and Housing Rehabilitation

The initiatives and enthusiastic participation to date of KFOR in humanitarian and rehabilitation activities are to be highly commended by the international community, and can serve as a good example for future collaboration in Kosovo, and elsewhere between peacekeeping forces and humanitarian agencies. KFOR's comprehensive coverage of Kosovo has made it a very useful source of information for which aid agencies can also benefit. By maintaining security throughout the region, and facilitating logistics where needed, KFOR greatly enhances the overall implementation capacity in Kosovo.

Logistical Constraints to Achieving Targets

28. Many agencies are already experiencing logistical difficulties in getting shelter and rehabilitation materials from sources to beneficiaries. With regard to imported materials, border crossing procedures should be smoothed. Rail and road improvement schemes would contribute to alleviation of logistics-related delays and bottlenecks. Increased local production of construction materials in the medium term would also ease the demands on the imports pipeline. Trucking capacity within Kosovo will have to be developed for movement of the large quantities of bulky materials required for a large-scale housing rehabilitation program in 2000. Meanwhile, a critical shortage of warehouse facilities restricts the extent and locations for significant pre-positioning and stockpiling of rehabilitation materials.

Urban Collective Housing

29. Collective blocks of flats, housing approximately 40 percent of the population of urban areas, suffered less damage in the conflict and thus may be in less desperate need of significant repairs in the coming months. In specific areas, however, flats have suffered heavy damage. Donor support is needed to ensure their rehabilitation, either through the use of private contractors, or by encouraging tenants to repair not only their flats, but also the common parts of the buildings (e.g., by providing construction materials). In some cases, assistance may be best used in helping households relocate, rather than in reconstructing severely damaged buildings.

30. In addition, most blocks of flats have suffered from severe degradation over the years, with little or no maintenance work undertaken. Experience in other Central and Eastern European countries indicates that the key to sustainable rehabilitation is the development of

appropriate mechanisms for management and funding of maintenance. Ownership issues must be addressed, which will require both making decisions on the current status of these flats (some of which belong to public companies-- the ownership of which is often contested), and passing legislation for the development of an appropriate regulatory framework (e.g., cooperative laws, etc.). Technical assistance may be needed to that effect.

Support to the Construction Industry Sector

31. The Kosovo construction industry sector must play a significant role in implementation of housing rehabilitation programs, whether these be donor-assisted or owner-funded, in addition to contracts for public buildings and infrastructure. Aid and private investments in housing and other physical rehabilitation works provide perhaps the greatest lever to relaunch Kosovo's economy. Vocational training schemes for carpenters and other building craftspeople will also be a very effective way of increasing the skilled workforce available to implement the large-scale rehabilitation work that is required.

32. Shelter and rehabilitation interventions in Kosovo have led to a major surge in demand for construction materials which cannot be met by the restricted supplies stocked by local traders. This imbalance between demand and local supply has resulted in (i) local retail prices rising significantly, with the unintended effect of making construction materials more costly for individuals who are financing their own home rehabilitation works, and (ii) most agencies importing building materials themselves from countries in the surrounding region. Urgent support to the recovery and expansion of the Kosovo construction materials industry must be a priority action. It would not only provide for job creation and import substitution, but could also help to control local prices, and to reduce freight movements on roads into Kosovo.

Other Issues

Registration of Ownership

33. Donor support should be provided for UNMIK and municipal authorities to put in place mechanisms for re-registration of ownership of housing property and land, especially where papers are missing as a result of the events of the last months. Mechanisms should be designed, under UNMIK's auspices, for both registration and dispute resolution so as to ensure maximal involvement of local communities and avoid unnecessarily heavy procedures. It may be that a simplified registration system should be adopted for the transition period. Technical assistance, as well as funding for operating costs of the appropriate institutions, are required for development of a cadaster so that houses can be properly registered, and in turn, serve as collateral and be bought and sold. Kosovars will be more encouraged to invest their own funds in housing if they are confident that there are no disputes over property ownership.

Planning and Regulatory Authorities

34. Support also needs to be provided through UNMIK to ensure that effective planning and regulatory authorities are in place at central and municipal levels, to control both rehabilitation and new building projects. The regulatory authorities will be involved in setting and monitoring construction standards, including for building safety. Urban authorities should also be supported in developing regulations and basic infrastructure, to prevent an uncontrolled development of cities as a result of rural migrations to urban areas.

Environmental Issues

35. In Kosovo and the surrounding countries, there is potentially a negative environmental impact from the large-scale procurement of construction timber, in addition to the firewood needed for distribution to vulnerable families for the winter. Timber is being procured from Montenegro, FYR Macedonia, Bulgaria and other neighboring countries, in addition to Kosovo itself. Consideration needs to be given to environmental protection measures and to compensatory afforestation-type projects that will alleviate any negative environmental impacts. This issue is discussed more at length in a separate annex on agriculture.

Box 2: Key Messages

- Coordinate housing aid programs with support to livelihoods, and rehabilitation of local infrastructure and utilities.
- *Manage* the transition from emergency shelter to rehabilitation.
- Target needy households, rather than damaged housing units, through fair and transparent targeting guidelines; communicate these guidelines to the population, and engage village communities in the application of agreed criteria.
- Monitor migration to urban areas for impact on the housing sector strategy.
- Use a variety of implementation mechanisms, including a voucher system for distribution of construction materials. Rely where possible on 'self-help' inputs by the beneficiary community. Engage the capacities of municipal authorities, NGOs and local contractors, the latter especially where the technical scope of repair work goes beyond what can be implemented by the beneficiaries.
- Support the recovery of the construction industry in Kosovo so that it is able to provide for a sustainable level of demand for construction materials, housing and other construction works.
- Provide support for building planning and regulatory authorities.
- Re-register housing property wherever titles were lost or destroyed.

C. COST ESTIMATES

36. The EC damage assessment report prepared by IMG provided a cost estimate of US\$1.06 billion for the rehabilitation of about 120,000 conflict-damaged housing units in Kosovo. A large part of this cost will however be covered through private resources. Estimates for external financing requirements (see Table 2 below) should therefore be based on the three following principles:

- Support should be limited to the rehabilitation of a 75 square meter habitable space per household;
- Support should be limited to the rehabilitation of housing units falling under IMG categories II, III and IV, with most inputs to categories III and IV; and
- Support should be targeted to most vulnerable households, with about 20 percent of the households in each of the categories II, III, and IV receiving assistance for both works and

materials, and another 40 percent receiving assistance for the provision of construction materials only.

Table 2: External Assistance Requirements for Private Housing Rehabilitation

EC/IMG Damage Category	I	II	III	IV
No. of housing units in the category	23,000	18,000	32,000	47,000
No. of households eligible for materials only (40 percent of total)	0	7,200	12,800	18,800
Cost per household (65 percent of total cost) in US\$	0	3,250	5,090	9,200
Subtotal in US\$ million (rounded)	-	23	65	173
No. of households eligible for both materials and labor (20 percent of total)	0	3,600	6,400	9,400
Cost per household in US\$	0	5,000	7,830	14,150
Subtotal in US\$ million (rounded)	0	18	50	133
Total cost in US\$ million (rounded):	0	41	115	306

37. Total external financing requirements for private housing rehabilitation amount to about US\$462 million for about 60,000 housing units, i.e. for about 500,000 people, at an assistance per person rate of about US\$924.

**Table 3: External Financing Requirements for the Housing Sector
(in millions of US dollars)**

Activity	First Phase (until December 2000)			Second Phase (2001-2003)	Total
	Until March 2000	April to Dec. 2000	Total		
INVESTMENTS					
Private Housing Rehabilitation	30.0	250.0	280.0	182.0	462.0
Collective Housing Rehabilitation	5.0	15.0	20.0	20.0	40.0
Subtotal	35.0	265.0	300.0	202.0	502.0
TECHNICAL ASSISTANCE					
Property Registration	0.0	5.0	5.0	10.0	15.0
Other	1.0	0.0	1.0	2.0	3.0
Subtotal	1.0	5.0	6.0	12.0	18.0
Total	36.0	270.0	306.0	214.0	520.0

ANNEX IV: WATER, SEWAGE, AND SOLID WASTE

A. SECTOR DESCRIPTION

1. Most of Kosovo's water supply systems are relatively small and cover the urban area of the municipality only (see Appendix):

- The six larger regional schemes, supplying water to one or more cities and nearby villages, serve in total 900,000 people (the number of consumers in these schemes varies from 80,000 to 250,000). These schemes use water from artificial storage lakes. Most of the systems were built in the 1970s and early 1980s and were constructed to meet increasing drinking water, as well as irrigation water demand. Water drawn from the storage lakes generally is filter treated before entering into the distribution system. However, due to lack of maintenance and incorrect dosing of chemicals, treatment is not always optimal, sometimes resulting in doubtful water quality. For disinfection reasons, spring as well as treated water is chlorinated before entering the supply system.
- About a dozen of small systems serve a total of 150,000 people; each system serves between 10,000 and 50,000 people (depending on the size of the city), with water usually drawn from boreholes and artesian springs. The quality of spring water generally is very good; boreholes however sometimes yield water of questionable quality, mainly due to heavy water pollution in adjacent rivers.

2. Rural water supply systems are almost non-existent. Most rural dwellings operate private wells or draw water from artesian springs. Rural wells generally are in bad condition and water quality is poor. The poor water quality is not always due to pollution of groundwater, but also to negligence of the users. Most wells are not protected, and surface water, dust and garbage find easy entrance into the well system. Moreover, many rural wells are very primitively operated by buckets that frequently do not meet any hygienic standard.

3. Most urban areas have combined wastewater and storm water collection systems, but the systems are old and badly maintained. Drainage channels are filled up with soil and debris and cause serious flooding problems during (heavy) rains. Sewer systems are of poor quality and frequently have broken pipes, allowing wastewater to infiltrate into the underground. Manholes are also in deplorable condition. Cast iron covers are frequently missing and have been replaced by concrete slabs, hampering traffic flow and exposing pedestrians to the danger of a fall at dark. During the last ten years hardly any of the networks have been extended to collect wastewater from new dwellings or even from newly-constructed, multi-storey buildings.

4. Wastewater treatment plants are non-existent in Kosovo. Apart from some very simple and hardly maintained industrial wastewater pre-treatment facilities, there is no other wastewater treatment. In order to avoid immediate danger to health, wastewater outlets are often located a few kilometers downstream of the city limits. Many riverbeds do not however carry any water during summer, and hygienic conditions in rivers downstream of urban areas are subsequently very poor. During the 1980s, wastewater treatment plants for the few bigger urban areas like Prishtine and Peja were designed, but construction was never started.

5. Villages and other settlements have no wastewater facilities at all. At most locations wastewater is being disposed of in open channels and sewage evaporates (in summer) or seeps

away into the underground. This causes contamination of groundwater, resulting in bad drinking water quality at the wells.

During the 1990s

6. After 1989, many high-level Albanian Kosovar managers, engineers and workmen were replaced or made redundant. The political tensions as well as the economic crisis in FRY put an end to the financial support provided by the central government to Kosovo, and by the provincial authorities to the municipalities:

- Only very little construction work was done in the 1990s to meet increasing water demand, caused by growth of the population (although master plans for new regional water supply systems had been developed and designed in the 1970s and 1980s). Urgently required extensions to the schemes were financed through a connection fee – but this fee hardly covered the real costs. And investments in source development and treatment facilities had to be postponed.
- Maintenance activities, leakage detection and repair were also reduced, resulting not only in a further deterioration of the distribution networks, but also in a rapid increase of unaccounted-for water.

As a result, water companies had to distribute available water over an increasing number of consumers. Over the decade, average (billed) consumption dropped by some 20 percent, further increasing the financial constraints of the water companies.

Post-conflict Situation

7. Physical damage as a direct result of conflict activities to the water collection and treatment facilities has been very limited in the urban supply systems. Only two pumping stations, a water treatment plant, and some civil structures at the water intake of a storage lake were reported to have received direct hits. Damage to the plumbing in burnt-out houses, however, causes serious problems. Since water companies are short of tools and parts to repair the leaks, water continues to run at many damaged locations. Also unreliable communications and lack of transport for the staff to and from the treatment facilities and pumping stations make operation of the scheme very difficult, resulting in severe interruptions in water distribution.

8. The situation in rural water supply is even worse. During the conflict, about half of the rural boreholes and wells were deliberately polluted, and returning refugees not only found their homes destroyed but also their access to clean water denied. Moreover, other wells, which were probably not polluted during the conflict, also need attention, since they have not been used for some time and been subject to pollution from dust and dirt. An estimated 15,000 to 20,000 wells are subject to cleaning and/or rehabilitation.

9. Adequate institutional frameworks for efficient operation and maintenance of the schemes are currently nonexistent. There is hardly any company structure and no proficiency to collect revenue. In the immediate aftermath of the conflict, a number of staff left Kosovo. Among other things, service vehicles, tools, protective clothing and remaining spare parts were lost. Vehicles and tools which were left behind are often out of order and certainly beyond cost-effective repair.

10. In some schemes, pre-1989 high-level staff have now resumed their former positions, but their skills are often outdated. In other schemes, where employees have been promoted to fill vacancies left by departing staff, lack of experience is even more tangible. The total collapse of the revenue collection system causes additional and severe financial constraints to the new management. Staff have generally not been paid for the last six months, and are leaving to find employment elsewhere. The lack of well-trained plumbers, indispensable for stopping the wastage in the network may cause additional problems in the near future.

11. The new management is progressing slowly in generating income. New tariffs (in DEM) have been developed and submitted to UNMIK for approval. Some water supply companies have started collecting payments at shops and other small economic activity sites, but, for obvious reasons, households have been spared thus far. Subsequently, results are very weak. It was understood that tariffs¹ cover the expense for operation and maintenance only, and that they do not cover depreciation.

Solid Waste Management

12. The solid waste situation is critical. There has been some progress in removing waste from the main thoroughfares in Kosovo cities, but in most places refuse continues to pile up. This is especially evident behind apartment buildings and in the peri-urban areas. Most of the trucks which handled containers have been lost or damaged. Additional and larger containers are urgently needed.

13. In Prishtine, waste management services are operated by the public company Hygenia Technica, which could stand independently as long as equipment and an operational budget are provided. Since June 1999, KFOR and NGOs have provided management, trucks and front end loaders to the city for collection. UNHCR has made available an additional 25 tipper trucks. UNDP has provided a US\$200,000 grant to sponsor an "I Love My City Prishtine" initiative – to purchase some equipment and pay 244 workers (prior to the conflict, there were 512 workers) for a 15 day period.

14. Prishtine's waste is disposed of at a site located approximately two kilometers from the city's periphery. Waste is deposited in an uncontrolled manner: there is no daily cover, there is no leachate treatment, the access road is not maintained, and recycling is done in an uncontrolled manner. The local pollution resulting from this dump is unknown since no sampling of nearby surface or groundwater has been done. For the long term, Prishtine will need two landfills, one in the east and one in the west. The currently used dump could be upgraded or re-engineered to provide another two to three years of capacity while alternative sites are sought.

15. In other cities, the situation is similar. Collection vehicles have been lost and management staff have left, resulting in unreliable service. Most refuse either piles up at intersections or is simply thrown into natural watercourses or drains. Many drains are full of refuse along with debris, which could result in major flooding-related problems in early Spring.

¹ A quick survey revealed that an average of DEM 0.25 per cubic meter would be applied to households, DEM 1.00 to institutions and DEM 1.50 to industries.

16. Medical waste is currently commingled with municipal waste. Hospitals are disposing of waste on-site, or simply throwing it in with other waste or attempting to burn it in pits. This waste contains sharps, syringes, bandages, blood-saturated wastes and body parts. All pose grave threats in exposing the public to blood-borne pathogens, and should be disposed of properly.

B. RECOVERY PRIORITIES

Water and Sewage

Objectives

17. The overall objectives are to: (i) improve the quality, reliability, efficiency and availability of the water supply, and upgrade the municipal and industrial wastewater collection; (ii) improve the operational and financial efficiency of the utility companies, and (iii) initiate a process for a sustainable development of the provision of municipal services in water and wastewater. To meet these objectives, feasibility studies will be needed to determine a priority investment program together with an institutional strengthening plan.

18. Standards for technical as well as financial performance should also be set up. Plans already exist to establish an association of water and sewerage enterprises in Kosovo, *the Kosovo Water and Sewerage Board*, to discuss common problems, work out strategies and define standards. Such plans have, however, not materialized yet, primarily because of the current vacancies in many utilities, but also because of the lack of experience of some of the newly-appointed managers. Also communication problems and lack of transport make the organization of such forum a difficult task.

Studies

19. A pre-feasibility study should be prepared as soon as possible to identify a short and medium-term investment program identifying viable projects to improve water and sewerage services, providing detailed cost estimates, and making recommendations on financing plans and tariff increases. The study will also look into the possibility of setting up twinning arrangements with other European water and sewerage companies, so that maximum use can be made of the available expertise and practical experience of these companies for support in operation and maintenance of the facilities, and the introduction of better services. It is proposed to finance the possible twinning arrangements under the technical assistance program.

20. The short- and medium-term investment program will take account of the following two stages:

- ***Stage 1:*** upgrading of water and sewerage facilities to pre-conflict level, comprising all necessary repair works to restore pre-February 1999 conditions. Since damage directly related to military operations has been rather limited, the scope of work for the program is not very large and of a simple nature. Most of the works could be finished within a few months time. Replacement of looted vehicles, tools, spare parts, pipes and fittings shall also be covered during this stage. First stage works do not include rehabilitation of neglected rural wells and are limited to interventions to damaged wells only. Minor repairs to damaged manholes in the sewerage schemes are also included.

- **Stage 2:** improved water service to all urban areas and upgrading of water treatment and distribution facilities to the pre-1989 level. The service will be based on a water consumption of 110-120 liter per capita and day, and will mainly comprise extensions to the distribution schemes to connect recently (since 1989) developed urban areas that have been deprived from access to piped water. Construction works will also cover extensions to present water treatment, storage and pumping facilities in some areas to meet the demand. During the second stage, it is intended to include rehabilitation of neglected rural wells. It is also intended to make a start with primary wastewater treatment (settling tanks and sludge disposal only) for approximately 400,000 inhabitants plus industry in the Greater Prishtine Urban Area when feasibility shows that primary treatment is viable and affordable.

21. Additional surveys will be needed, in particular to:

- develop an affordable, least cost investment program for the short-term, i.e. spring 2000 to spring 2001, and long-term, i.e. spring 2001 to spring 2003, including procurement and implementation schedules and potential risk analyses; and
- lay the foundation for a process that will transform the water companies into a modern service-oriented water supply and, if applicable, sewerage utility, which will be run commercially and in accordance with modern utility management practices. Private sector participation options such as service contracts, management contracts, concessions (lease contracts) and BOT (Build, Operate, Transfer) shall be investigated. After completion of the process, the water companies shall be self-sufficient without reliance on government subsidies, providing a quality service at an affordable price. The implementation of the improvement program shall be parallel to the execution of the feasibility study.

Project Implementation

Phase I: Fall 1999- Spring 2000

22. Following the time schedule of the proposed studies, detailed information on viable and sustainable investments that are in line with future expansions of the water companies will be available after completion of the feasibility study, i.e. approximately 5 months after start-up of the studies. The Kreditanstalt fuer Wiederaufbau (KfW) of Germany is presently preparing feasibility studies on water supply systems in almost all cities. Hence, results of the study might already be available at an earlier date. Furthermore, KfW is active in Prizreni and also intends to get involved in the Rahoveci Water Supply Scheme.

23. Emergency measures should be taken as rapidly as possible, to: (i) enable the water companies to continue operating the water supply facilities, reduce the wastage and start collection of revenue, so as to ensure access of urban population to safe drinking water; (ii) complete the cleaning-up and rehabilitation of rural wells and boreholes, currently underway (with support by a number of NGOs); (iii) provide urgent Technical Assistance to the companies in organizing network rehabilitation and water billing, as well as training courses for the management; (iv) cover operating costs for the provision of chemicals and spare parts as well as for paying wages and power bills; and (v) introduce a proper billing system to ensure some cost recovery. Details of the program are shown in Appendix 2.

24. The most urgently required need during this phase is the financing of *salaries* during a period of approximately six months. By the end of this period, water companies will have completed the process of reestablishing meter reading and billing, and will be able to pay for salaries and some other operation costs. For the coming winter most urgent repair works shall have to be finished and for this purpose *tools, spare parts, pipes and fittings* are needed urgently. Procurement delays for the spare and fittings are not justifiable. To ensure safe water quality over winter, *chemicals* for flocculation and chlorine for disinfection are also urgently required.

25. Presently operation of water treatment plants, pumping stations and storage facilities is severely hampered by lack of transport. Also repair works can only be performed on a limited scale due to lack of *vehicles*. Procurement of vehicles is to be completed before winter. As an alternative to procurement, it may also be envisaged to rent or lease transport or sublet the activities to private companies. The *rural well cleaning* program is well on its way, but needs to be completed as rapidly as possible.

26. Emergency aid (provision of cars, tools, spares, fittings, etc.) is presently being granted by numerous NGOs, and organizations such as DFID, SDC, KfW, and Vivendi. Although there are still a number of needs which are unmet, NGOs are getting increasingly active in the field and it may be assumed that after a period of six months, most urgent needs for goods and works will have been covered.

27. Efforts should also be made to re-start billing to collect revenue. Water companies generally have good understanding of required tariffs to cover operation and maintenance costs, but present (FRY) legislation demands political approval before tariffs can be applied. Tariffs have already been submitted to UNMIK for approval. During the next six months, however, the water companies will need restricted financial support for salary payments to encourage the staff to rapidly carry out required repair works. The financial support should phase out over the period, ensuring that management will have sufficiently prepared for collection of revenue.

Phase II: Spring to end 2000

28. Phase II will be characterized by large rehabilitation and repair works comprising: leak repair programs in the distribution networks; reconditioning of water treatment; pumping and storage facilities; meter repair and calibration; and sewer manhole and pipe repair already initiated in Phase I. The program will also cover outstanding maintenance works and will obviously slip far into phase III before completion.

29. An immediate start shall be made with the *rehabilitation of the treatment, pumping and storage facilities* in all schemes. It was noted that conflict damage in the Western part of the Province, comprising the cities of Peja, Gjakova, Rahoveci, is more significant than at other places. Numerous dwellings were set fire to, and private house connections and *network repair* seems to be more substantial than elsewhere. It was also observed that sewage collection systems in these cities have also suffered from conflict damage. Manholes and house connections have been filled with debris and rubble. The cleaning of the *wastewater collection networks* shall not be delayed, and shall start in the beginning of phase II. Physical water losses are unacceptably high in the Province. The phase II rehabilitation program includes supply of equipment to better monitor the production and distribution of water. *Telemetry and (bulk) water meters* are part of the procurement plan.

30. Finally, the program also comprises delivery of *computer hardware and software*. Although it was noted that most financial departments in water companies operate computers, the equipment is old, not always properly functioning and needs replacement. New equipment will also contribute to tighter control on water consumption and billing.

31. Since there is neither adequate institutional framework for efficient operation and maintenance of the facilities, nor for preparation and supervision of the reconstruction programs, technical assistance will be required to meet the objectives.

Phase III: 2001 to 2003

32. During this phase, rehabilitation works and extension works will be completed, and will include: (i) rehabilitation of the treatment, pumping and storage facilities; (ii) water distribution network repair; (iii) wastewater collection networks; (iv) telemetry and (bulk) water meters; and (v) computer hardware and software. During that period, identified privatization projects and required managerial/organizational changes will have to be implemented through technical assistance programs.

Institutional and Financial Requirements

33. The water companies, once provided with the required tools and spares, should be able to manage urgent repairs without technical assistance. Also re-start of water consumption billing can be easily performed by existing organizational structures. However, without assistance, it will not be possible to prepare and supervise major rehabilitation works, conduct procurement of works and goods, as well as transform the water companies into modern service-oriented water supply and, if applicable, sewerage utilities, which will be run commercially and in accordance with modern utility management practices.

34. Such assistance could possibly be provided through twinning arrangements with West European water utilities with a view to make available optimal practical experience for assistance in carrying out rehabilitation works and procurement of goods. Such twinning arrangements would provide direct access to in-depth knowledge and experience in procurement of goods and works through the partner company. Moreover, through twinning arrangements the first steps can be made toward private sector participation.

35. For the implementation of the financial and operational performance improvement program, an overall strategic plan for future development of the water companies should be formulated. This plan will: (i) make explicit the fundamental objectives for the transformation of the companies, (ii) define the appropriate legal and regulatory framework for the relationship between the water companies and the local and provincial government; and (iii) outline main steps toward private sector participation. All water companies should probably not be transformed into joint stock companies. On the contrary, probably only the Batlava System with an approximate number of people connected of 300,000-400,000, and the Grazivoda System with some 200,000-220,000 people connected, may be subject to privatization, whereas all other water companies may only be interested in private sector participation.

36. Technical assistance for all companies will furthermore focus on the introduction of international accounting principles, preparation of business plans that will include operational performance (leakage control), cost control, investment program, tariff levels, service quality, etc. In general, the smaller companies may have sufficient experience in operating the schemes,

but they lack financial and institutional expertise to properly handle extensions works, and larger rehabilitation measures, or to improve financial viability.

Solid Waste Management

37. Significant donor support is needed, to improve solid waste management, including:

- Vehicles and equipment. Estimates for Prishtine vary widely, but there is a consensus that the city needs another 15 to 20 vehicles, roughly 1,000 one m³ bins and a couple hundred 5 to 7 m³ bins, and other types of specialized vehicles. A one-year program should be implemented to re-engineer the landfill. In other cities, a total of some 11,000 small and 2,000 large containers are needed, as well as 150 vehicles. Support should be provided in several tranches, after an in-depth survey has been carried out (this is currently under way by IMG). Additional support will be needed to construct a dozen landfills outside most of Kosovo's major cities.
- A centrally located incinerator for medical waste at the largest hospital complex in Prishtine. This incinerator could serve Prishtine's seven main hospitals operating at 350 to 400 kg/h. The unit would operate around the clock, would include a two-stage combustion system, an ash handling system (ash would be landfilled), and air pollution control. These types of package incinerators are used routinely at hospitals and other facilities producing small quantities of red bag wastes. They are generally small and pose no environmental threat.
- Rubble crushers for debris. About 120,000 housing units suffered heavy damage. Much debris remains on the streets of small towns, large cities as well as at many isolated, rural home sites. This material will be shoved aside, much of it into drains and water courses, but some of it should be recycled for construction material. To that effect, it needs to be sized into aggregate by means of rubble crushers and classifiers. Currently there are three such machines in Kosovo, but at least six to ten mobile units are needed.
- Operating support for the collection and disposal of refuse, to get the city through the winter. This requires approximately US\$200,000/month for salaries (see below), operating costs (fuel, especially) and spares. Cost recovery mechanisms should be developed during this initial period. A related technical assistance program is also recommended, in particular in areas of contract management, budgeting, equipment leasing and purchasing, equipment maintenance, landfill operations and solid waste planning.

C. COST ESTIMATES

38. Some cost estimates have been obtained from IMG, others derived from reports of surveys in other schemes. By applying derived cost factors of the available information to the data obtained from other sources on other schemes, tentative cost estimates have been developed. More precise cost estimates will be available after completion of the pre-appraisal study.

**Table 1: External Financing Requirements for the Water Sector
(in millions of US dollars)**

Activity	First Phase (until December 2000)			Second Phase (2001-2003)	Total
	Until March 2000	April to Dec. 2000	Total		
WATER AND SEWAGE					
Investments	0.0	0.0	0.0	0.0	0.0
Rural Well Rehabilitation and Cleaning	3.0	1.0	4.0	0.0	4.0
Vehicles	15.0	1.0	16.0	5.0	21.0
Rehabilitation of Water Schemes	0.0	20.0	20.0	33.5	53.5
Extension to Water Schemes	0.0	6.0	6.0	65.0	71.0
Rehabilitation of Sewerage Schemes	0.0	2.0	2.0	2.0	4.0
Extension to Sewerage Schemes	0.0	5.0	5.0	18.0	23.0
Primary Wastewater Treatment and Collectors	0.0	5.0	5.0	25.0	30.0
TECHNICAL ASSISTANCE					
Technical Assistance to utilities	1.8	3.5	5.3	6.0	11.3
Studies	2.0	0.0	2.0	0.0	2.0
Subtotal	21.8	43.5	65.3	154.5	219.8
WASTE MANAGEMENT					
Investment	0.0	0.0	0.0	0.0	0.0
Urgent Vehicles	1.5	0.0	1.5	0.0	1.5
Vehicles, Equipment, Landfill re-engineering	2.0	7.0	9.0	25.0	34.0
Hospital Incinerator	0.0	1.5	1.5	0.0	1.5
Rubble crushers	1.2	0.0	1.2	0.0	1.2
Technical Assistance	0.1	0.0	0.1	0.0	0.1
Subtotal	4.8	8.5	13.3	25.0	38.3
Total²	26.6	52.0	78.6	179.5	258.1

² In addition, about US\$11.7 million will have to be funded through the budget for operating expenditures in the sector.

APPENDIX: OVERVIEW OF THE MAIN WATER SUPPLY SCHEMES IN KOSOVO

1. **Batlava System**
Approximate number of people connected: 244,000.
Major cities connected: Prishtine, Podujeva, Gracanica, Obiliqi.
2. **Grazivoda System**
Approximate number of people connected: 165,000.
Major cities connected: Mitrovica, Zvecan, Vushtrija, Skenderaj.
3. **Prizreni System**
Approximate number of people connected: 165,000.
Major cities connected: Prizreni
4. **Radonic System**
Approximate number of people connected: 120,000-160,000.
Major cities connected: Gjakova, Rahoveci.
5. **Peja System**
Approximate number of people connected: 100,000-120,000.
Major cities connected: Peja
6. **Gjilani System**
Approximate number of people connected: 80,000-90,000.
Major cities connected: Gjilani
7. **Ferizaji System**
Approximate number of people connected: 40,000-45,000.
Major cities connected: Ferizaji
8. **Suhareka System**
Approximate number of people connected: 25,000-27,000.
Major cities connected: Suhareka
9. **Istogu System**
Approximate number of people connected: 15,000.
Major cities connected: Istogu
10. **Glogoci System**
Approximate number of people connected: 11,000-12,000.
Major cities connected: Glogoci
11. **Kamenica System**
Approximate number of people connected: 10,000-12,000.
Major cities connected: Kamenica
12. **Lipjani System**
Approximate number of people connected: 10,000-11,000.
Major cities connected: Lipjani

13. **Kacaniku System**

Approximate number of people connected: 10,000-11,000.

Major cities connected: Kacaniku

14. **Leposaviqi System**

Approximate number of people connected: 10,000.

Major cities connected: Leposaviqi

15. **Klina System**

Approximate number of people connected: 8,000.

Major cities connected: Klina

16. **Decani System**

Approximate number of people connected: 5,000.

Major cities connected: Decani

17. **Vitija System**

Approximate number of people connected: 3,500.

Major cities connected: Vitija

ANNEX V: LANDMINE CLEARING

1. Before the recent conflict erupted in Kosovo, the province was uncontaminated by landmines, booby-traps, and unexploded ordnance (UXO). Unlike in other areas of Europe, no explosive materials had been laid during the two World Wars. The inhabitants of Kosovo were therefore unaware of the dangers of landmines and UXO. In spite of the danger, and in defiance of the advice of the international community, 800,000 refugees spontaneously returned to the province in June as KFOR forces moved in. At the time, there was no data available regarding landmine and UXO contamination. However, during the refugee crisis, UNHCR coordinated a massive landmine awareness campaign in asylum countries and at the borders. The toll paid for the spontaneous and non-advised return was relatively limited with 232 casualties, of which 40 were fatal (from June 12 to August 31, 1999). Most of the refugees had returned to Kosovo by the end of August and were trying to resume productive activities (e.g., house reconstruction, farming). Up to 25 percent of those activities are directly affected by the presence of landmines and UXO.

2. Lack of funds has been a key contributing factor to the very slow pace of recent demining programs in the region (Croatia and Bosnia and Herzegovina), and this issue has received large media coverage. As a result, more attention, and more financing, allowed very prompt assistance since the very beginning of the humanitarian operations in Kosovo. If current financing levels continue without break, it is expected that the landmine and UXO problem could be eliminated in three years. This Sectoral Annex presents a three-year, US\$32 million program to accompany the efforts that have been made so far to eradicate landmines and UXO in the province.

A. SECTOR DESCRIPTION

3. The Socialist Federal Republic of Yugoslavia (SFRY) was one of the main manufacturers and exporters of anti-personnel and anti-tank mines. However, this production expertise was not matched by capacity in demining. As was the case in both Croatia and Bosnia and Herzegovina, a few army platoons were trained to deal with UXO and carried out basic demining, primarily in order to clear passages into battlefields during combat. As of today, the few skilled deminers who did exist have left the province.

4. Kosovo represents the smallest area of territory affected by landmines in the world: Prishtine is less than a two-hour drive from any location in the province. The limited size of Kosovo has been key to the satisfactory setup of the coordination and information management systems put into place under the auspices of the United Nations Interim Administration Mission in Kosovo / Mine Action Co-ordination Center (the MACC). Today, less than three months after the international community arrived, the first emergency phase is being implemented. Institutions are in place, NGOs and contractors are carrying out a wide variety of actions to address the landmine and UXO problem. A total of 16 organizations are working on the problem-- a number which is unequalled in other problem areas worldwide. Initial statistics on the extent of contamination are now available. The army of the Federal Republic of Yugoslavia (FRY, VJ forces) has provided records for 616 mined areas, and NATO has identified 333 cluster bomb drop-sites on which a total of 1400 bombs were dropped. As part of the peace settlement, the Kosovo Liberation Army (KLA) has removed the mines they used during the conflict. All in all, 1000 suspected mined areas have been reported, but 30 percent of the casualties that have been reported occurred in other locations. This indicates that: (i) it is critical that the existing database continues to be expanded by gathering information, and (ii) nuisance mines placed in and around many villages have not yet been reported.

Table 1. NGOs and Private firms present in Kosovo as of September 15, 1999

NGOs	Staff	Contractors	Staff
HALO Trust	20	BACTEC	10
HELP	75	European Landmine Solution	10
Mine Advisory Group	80	Defense Limited Systems	55
Norwegian People's Aid	25	Minetech	60
Handicap International	15	Ronco	85
Danish Church Aid	35	IDAC	30
Wolfs Flats	10	Gerbera	10
Inter SOS	30	Emercom	20
Total	290		280

5. In general, the danger which landmines and UXO pose can be characterized in three distinctive cases:

- The VJ forces laid minefields both to defend the provincial borders and to protect their defensive positions. They also laid mines in and around some villages in order to limit the movements of the KLA forces;
- The KLA forces laid some mines, which, as part of a negotiated agreement, they were to remove. The KLA reported that they had completed this task, but they did not provide records;
- NATO aircraft dropped Cluster Bomb Units (CBU), which is the major type of UXO contamination.

6. The United Nations Mission in Kosovo (UNMIK) was established on June 10, 1999. The United Nations has selected the UN Office for Project Services (UNOPS) to implement the UNMIK Mine Action Program (the MAP) on its behalf, initially through funds made available from the Voluntary Trust Fund for Assistance in Mine Action (the VTF). At the same time the MACC was established in Prishtine as the focal point for the MAP.¹ The MAP responded to the immediate needs of returnees, by providing guidance, identifying needs and priorities, and coordinating with partners (e.g., EU, UNHCR, UNICEF, WHO, WFP, NGOs, KFOR and ICRC). The MAP developed rapidly. Three phases were identified:

- *The preliminary phase*, which was completed by July 1999, included: (i) a mine awareness campaign in refugee camps; (ii) a rapid assessment of landmine/UXO contamination; (iii) the development of a mine victim surveillance system and; (iv) the establishment of the MACC (6 expatriates and 20 local staff);
- *The emergency phase*, which will end by December 1999, in which 16 NGOs and contractors provided resources to address survey, mine clearance and mine awareness needs. As of August 31, 1999, three thousand houses were cleared, and 350 local deminers were attending training. This demining capacity was funded by US\$12 million

¹ The MACC coordinated with UN partners (UNHCR, UNICEF, WHO and WFP in particular), non-UN partners (NGO, KFOR, GIC and ICRC in particular), and Member States. The MACC defined the overall operational plan and structure required to coordinate mine action activities throughout the province.

in commitments from the donor community through bilateral mechanisms or through the VTF²;

- *The consolidation phase*, which will overlap with the emergency phase by the end of 1999, and which will focus on mine action activities which can continue during the winter, and on the preparation of the next demining season (starting in March 2000) and beyond.

7. The first consolidated database of minefields and UXO location was established by the end of August 1999, thanks to the fruitful transfer of information from KFOR to the MACC³, and to the initial survey of 1,000 of the 1,900 towns and villages in Kosovo (made by HALO Trust). The survey concluded that there was low mine density in populated areas, but that contamination was widespread. In August, the Survey Action Center (managed by the Vietnam Veterans of America Foundation) conducted an additional survey in which existing information was compared. The results of this study, which will be released at the end of September, will provide the MACC with updated information which could be published in the winter. Detailed surveys have not yet been conducted, which is understandable due to the very short lapse of time since operations were initiated. Only a very small percentage of suspected minefields are marked, e.g., with colored plastic fences.

8. The emergency phase has enabled vital support for the return of refugees and internally displaced populations to Kosovo. Implementers of landmine and UXO related programs are expanding their operations using lessons learned thus far. The MACC is currently adding Quality Assurance capability to its promising existing structure. Quality Assurance would certify land once demining is completed. More survey equipment should be operational soon, and an assessment of the performance of the 16 operational NGOs and contractors to date will help maximize the effects of existing programs.

B. SECTORAL PRIORITIES FOR RECOVERY

9. Thanks to the MACC, the sector already benefits from the existence of a Mine Action Program. The Mine Action Program establishes clearly what action needs to be taken, thereby ensuring consistency and optimal coordination.

Program Objectives

10. Clearance of strategic sites is crucial to the rehabilitation of infrastructure, to economic recovery, and to the return of refugees and internally displaced populations. Mine actions are not

² Among the identified donors, the European Union, Luxembourg, Norway, and the United Kingdom contributed through the UN Trust Fund, while Belgium, Canada, Denmark, France, Spain and Switzerland have pledged funds. Canada, Denmark, Italy, Germany, United Kingdom, United States, Slovenia, Sweden, Switzerland and New Zealand contributed using bilateral mechanisms.

³ The Information Management System for Mine Action (IMSMA), which has been developed for the UN by the Government of Switzerland, was initially deployed into Kosovo under KFOR auspices. The MACC have subsequently assumed responsibility for the ongoing management of the database, which provides an essential tool for information collation, analysis, storage and dissemination. Such a system greatly enhances the ability of the MACC to prioritize all mine action activities, and to effectively coordinate the collective efforts of the various organizations. The MACC intends to deploy ten read-only versions of the system to regional locations in order to improve accessibility to the data across the province.

considered a stand-alone activity, and it is crucial that the program be woven into all facets of the recovery process. The goal of donor contributions is to help consolidate the results achieved in the emergency phase described above, which will ensure implementation sustainability in the medium-term. Simultaneously, some of the arrangements set up during the emergency phase need to be adjusted. The objectives of the consolidation phase are three-fold:

- a) *The return of land free of landmine and UXO for humanitarian and reconstruction purposes.* It is estimated that all settlements and their vicinities could be free of landmines and UXO by December 2000, and that all minefields and bomb-contaminated areas could be cleared by December 2002.⁴ Demining is a fundamentally humanitarian task of the utmost urgency for Kosovo because of its implications for public safety and socio-economic development. The importance of a flawless success rate is self-evident in mine clearing, as the existence of a single mine will destroy the land user's confidence. Specific efforts are requested so that all demining activities are conducted—and recorded—according to United Nation Humanitarian Demining Standards.⁵
- b) *Increased public awareness of the existing dangers of landmines, booby-traps and UXO.* In the consolidation phase, mine awareness education programs should be pursued to limit the risk of accidents. Mine awareness programs would be a very efficient and low-cost means of limiting the number of future accidents over the next two years. There is a correlation between the recent decrease in the number of casualties (86 in June; 118 in July; 28 in August), and the fact that most of the refugees had returned to their land by the end of August 1999. Nevertheless, a large proportion of the population is still camping near their house and/or do not have access to the surrounding areas. Furthermore, it is estimated that 30 percent of the accidents that occurred could have been avoided if routine precautions had been respected (especially regarding BLU 97 and RBL 755 cluster bombs, most of which are still not detonated).
- c) *Assistance to mine victims:* The program should provide appropriate medical support and rehabilitation facilities to cope with the situation and help the victims to reintegrate into society. Fortunately, to date a relatively small number of people have been maimed by landmines since June 1999. Nevertheless, there is still no mechanism in place to mitigate the impact of mine accidents.

Program Description

11. The above mentioned objectives will be met under the condition that continuous efforts are made to support the actions implemented under the existing setup, and if some adjustments are made.

⁴ Although minefields along the borders and around VJ forces' compounds (representing about 20 percent of the suspected minefields) are expected to be cleared within this period by VJ forces, there is no schedule available for those activities yet.

⁵ Humanitarian demining standards provide a framework for the creation of Standard Operating Procedures (SOPs), which in turn detail the manner in which specific mine clearance operations are conducted. Examples of SOPs and guideline documents can be obtained from the UN Mine Action Service, UNMAS, United Nations, New York, NY 10017 USA or @ www.un.org/depts/landmine

Support for actions implemented under the existing setup:

12. **Mine Clearing Operations.** Most of the actions that were implemented in the emergency phase will be continued as part of the Program for the following years. The NGOs and contractors involved in landmine/UXO clearing will continue verification/survey tasks, mine /UXO clearance of houses, key installation and clearance of priority areas, ongoing mine awareness programs, and development of a victim assistance program. Re-evaluation of objectives conducted at the end of 1999 by the MACC may result in re-configuration and/or changes in the command and control arrangements upon which the consolidation phase will be developed (see adjustments below).

13. **Mine Awareness.** Mine awareness activities in the consolidation phase will be based on formal / non-formal education. Formal education will include developing a school-based curriculum through UNICEF (already financed) and a civil police curriculum which will become part of the Kosovo Police Academy curriculum to improve reporting and mine awareness capacity through the community policing system. Non-formal education will target community-based activities (child-to-child education, safer village plan). Training for health monitors and religious leaders is also planned, as is sponsoring youth clubs which use mine- awareness messages. The information contained in the MACC database, when verified, should be broadly disseminated so that local communities can be aware of the locations of suspected minefields.

14. **Mine Victim Assistance.** Efforts need to be made to develop landmine victim assistance programs. These programs, which have not yet been established in Kosovo, should begin with emergency medical aid in the form of upgrading facilities which deal with traumatic amputations and specialist services (i.e., physiotherapy, and psychotherapy). Once facilities are upgraded, the reintegration of victims into society needs to be monitored, including the provision of prosthetics and the re-training/re-employment of victims, with the ultimate goal of reintegrating them into their former workplace.

Adjustments to the Existing Setup:

15. **Verification of Suspected Contaminated Areas.** The principal additional feature that needs to be implemented under the Program is verification of the suspected contaminated areas (called a survey level two campaign). Demining is very time consuming and expensive. It is therefore important to carry out a detailed and well-documented survey of the extent of contaminated areas before too many resources are used for actual mine and UXO clearing operations. Mapping and marking dangerous areas would also help to curtail the fear the local population has of suspected areas. Well-documented databases should also be disseminated locally in an effort to inform local communities about the presence of minefields. United Nations statistics show that in 1996, under UN mine clearing programs world-wide 25 square kms were restored for habitation as compared to 1,000 square kms declared free of mines through verification using survey level two methodology. This demonstrates the tremendous impact such a survey could have on the cost and efficiency of a well-conducted landmine and UXO action program (mine clearing techniques are exponentially more expensive than verification techniques). There is a need to verify that there is no mine without using the traditional prodding technique. Communication with local sources, use of trained dogs, and use of relatively light equipment are necessary tools for verification. Subject to confirmation during the implementation of the survey level two campaign, it is estimated by the MACC that 60 percent of current suspected contaminated areas could be declared free of mines when the campaign is complete.

16. **Further Development of the List of Priorities, and Coordination with the Other Sectors.** This second adjustment would aim at improving prioritization of needs and setup arrangements so that demining actions could be launched on-demand as the various reconstruction sectors develop. Current operations provided significant on-demand capacity to the refugees during the emergency phase, but future operations should be based on a list of priorities. Economic benefits and/or humanitarian benefits that are expected from cleared areas should be decisive factors in the selection of sites to be demined. The MACC should also coordinate with other sectors to discuss their priorities, so that on-demand demining capacity could be available when warranted.

17. **Performance of the 16 NGOs or Private Firms.** There are lessons to be learned from the emergency phase, regarding the performances of the 16 NGOs or private firms that are present in Kosovo in landmine/UXO related project implementation. The capacities of the organizations varies (from 4 to more than 100 staff), as do their methods, equipment and core programs. The current arrangements need to be revised, both the geographical repartition and the distribution of tasks—in order for the objectives of the consolidation phase to be met, and to ensure that there is no duplication of efforts or reduction of benefits. Emphasis should be given to supporting organizations to develop integrated capabilities, i.e., organizations that have enough capacity to have both survey and clearance teams. Mine awareness initiatives in the consolidation phase should be rationalized, as too many actors are currently involved in program work (16 as of August 31, 1999). Current activities should be integrated into the overall operational plan.

Box 1: Some Specific Needs Under the Program

- (i) The emergency phase has brought equipment for deminers to Kosovo, including protective suits and metal detectors. However, equipment which would enable conducting sound level two operations (mini flails, vegetation cutters, marking material) is still lacking. Increased use of mine-detecting dogs would be welcome;
- (ii) Material to disseminate landmine and UXO database information to local communities and promote awareness programs through the media (e.g., sponsoring a radio soap opera on local networks; television advertisements; development of specific reporting information; child-oriented posters, school books etc);
- (iii) Assistance to mine victims (e.g., evolving orthopedics for children, development of a victim register which can follow up on individual cases, sponsor capacity in local prosthetic management workshop, sponsor physio- and psycho – social services).

Implementation Arrangements

18. Coordination and appropriate division of tasks between intervening institutions is crucial. The MACC is the central authority for the development of mine clearance strategy and its implementation. The MACC will coordinate the assistance provided by the donors rather than implement mine action activities itself. The MACC will continue accrediting the organizations where appropriate, and will ensure that all works are conducted within the context of a sound action plan agreed upon with the donors. The MACC will continue to liaise regularly with all those involved --especially organizations in charge of the sectors under the recovery program-- and provide a prioritized list of sites for clearance of landmines and UXO, and on-demand demining capacity to the sectors. This effort will guarantee that the demining program will not

divert from other reconstruction efforts. Each sector should finance demining activities necessary for future investments under a standard protocol between them and the MACC which will offer guaranteed accountability and ensure that fund use is transparent. The MACC should also continue providing implementation assistance to the mine awareness program for which UNICEF is the focal point. Although mine victim assistance surveillance and assistance will be implemented under the auspices of WHO and ICRC, the responsibility for integration of related activities to the overall program will remain with the MACC.

19. There is still room for improvement in the division of tasks between organizations by geographical sectors so to ease logistic problems. However, the distribution of demining tasks should be consistent with the priority needs of the consolidation phase i.e., survey level two including marking, UXO clearance including cluster bombs, humanitarian demining and demining on-demand for the sectoral programs. As a result some organizations might work within the same territory; others that are not skilled enough, or sufficiently staffed, should be phased-out.

20. As the initiator responsible for the implementation and coordination of the Program, the MACC has to report to the donors on the use of their contributions. The MACC should therefore be able to assess whether the cost of demining, which is by far the most expensive activity to implement is acceptable. Discussion of average prices per square meter is always extremely controversial for this activity, and contractors are very reluctant to consider using such an approach. In spite of this attitude, the cost of demining activities in the province should be compared with the cost of similar operations in Croatia and Bosnia and Herzegovina. The salaries of deminers in the province are 30 percent lower than in Croatia and Bosnia and Herzegovina, and a significant portion of the work, i.e., clearing of cluster bombs, is expected to cost less than traditional demining. Based on this, it is recommended that operations for which the average cost per square meters is above average prices in Croatia or Bosnia and Herzegovina⁶ be audited and/or retrofitted.

21. VJ forces will have a role to play in the demining efforts throughout the province. Under the terms of the Military Technical Agreement, VJ forces are required to mark and clear minefields, booby-traps and obstacles. KFOR and VJ forces are preparing a detailed plan for these activities province-wide. The plan will also include sites not included in the priority list (e.g., minefields laid around defensive positions or by the border of the province) which could be cleared by VJ forces over the three-year program

External Financing Requirements

22. The institutional setup mentioned above, the demining capacity as well as the mine awareness campaign and mine victims assistance program will need continuous support over the next three years. The manner in which funds are released will be critical to the Project, as lack of financing or non-guaranteed short-term funding would lead to the withdrawal of demining teams and the attendant loss of their trained capacity. The VTF could be an effective means to provide resources to existing institutions, and to finance humanitarian relief, and should be considered as a prime mechanism.

⁶ In Croatia, the average price including all type of terrain stabilized around 2.5 - 3 DEM per square meter (after an initial phase, in 1997, where it was as high as 5 to 6 DEM per square meter). In Bosnia and Herzegovina prices were up to 9 DEM per square meter in 1997. They have currently stabilized at around 3 DEM per square meters.

**Table 2: External Financing Requirements for Landmine Removal
(in millions of US dollars)**

Activity	First Phase (until December 2000)			Second Phase (2001-2003)	Total
	Until March 2000	April to Dec. 2000	Total		
INVESTMENTS					
Survey Level Two Operations	3.0	5.5	8.5	0.5	9.0
Landmine and UXO Clearing and Other Related Tasks	2.0	5.3	7.3	7.2	14.5
Mine Awareness	0.8	1.2	2.0	0.7	2.7
Mine Victim Assistance	0.3	0.5	0.8	0.6	1.4
Support to UNMAC	0.9	1.5	2.4	0.0	2.4
Total⁷	7.0	14.0	21.0	9.0	30.0

Policy Requirements

23. Policy requirements under the Program are related to the management of local manpower in demining activities. There are three areas of concern:

- The salary of the local deminers should reflect the trend for similar employment in the province, taking into account the specificity of demining activities. All organizations currently pay the same salary, i.e., 800DEM per month, and provide more or less the same level of insurance coverage for the workers (350DEM per month). This salary is considered fair by the firms, but is contested by the workers.
- In the year 2000, there will be some 350 locally trained deminers-- most of them former KLA soldiers. Unlike other programs in the world, there is no need in Kosovo for a sustainable local demining force. Therefore, because the Program is expected to be completed by December 2002, the question of the redeployment and retraining of demining personnel needs to be addressed while the program is still in operation. Additional consideration will need to be given to the future integration of the Kosovo Protection Corps.
- The action plan regarding demining activities to be conducted by VJ forces is not yet available. Conditions to initiate this component should be identified and met, so that mapping, marking and clearing operations by VJ forces can start in 2000.

⁷ In addition, about US\$4.5 million will have to be funded through the budget for operating expenditures in the sector.

ANNEX VI: EDUCATION

A. SECTOR DESCRIPTION

Description of the Education Sector: Pre-1989 and Recent History (1990-99)

1. Beginning with its creation in 1945, the Socialist Federal Republic of Yugoslavia was a positive force for Kosovar Albanians in terms of access to Albanian language education. Prior to the World War II, education in the province of Kosovo was conducted almost exclusively in the Serbian language, and at the time of the creation of SFRY, nearly three quarters of adult Kosovar Albanians were estimated to be illiterate. Albanian language enrollments rose steadily under SFRY, with a dramatic increase in the ten years beginning in 1968, when the proportion of Kosovar Albanians in the region's education system rose from 38 to 72 percent.¹ The University of Prishtine (formerly a branch of the University of Belgrade) was created in 1969, and enrollments in Albanian language higher education programs experienced a similarly dramatic increase. Illiteracy among the adult population is said to have decreased to well under 10 percent, but may have begun to increase again during the past decade.

2. Although access was increasing dramatically, local influence and control over education content was not. The federalist 1974 constitutional reforms gave the mixed population of Kosovo theoretical control over nearly all education governance and content matters, and Kosovar Albanians were empowered and emboldened to promote their own culture and history through education. As a backlash against the outcome of these federalist reforms – which led to serious university student demonstrations in 1981 -- authorities in Belgrade moved to re-centralize control over educational content during the 1980s, finally transferring all authority for it to Belgrade, with the abolition of Kosovo's formal autonomy and the adoption of the 1990 Serbian constitution – events which led to creation of the “parallel” system in education. It is important to note that while control over curriculum content, particularly in history and cultural subjects, is central to the conflict in Kosovo, a strong system of decentralized management and financing of the education system was in place in SFRY. The Kosovar Albanians did participate in this fiscally devolved system and, to some extent, controlled the management and financing of general education in many majority Kosovar Albanian municipalities prior to 1989.

3. In 1991-92, the majority of Kosovar Albanian students left the formal FRY-supported education system. Although formal, government-supported salaries were discontinued, the education of Kosovar Albanians, representing about 90 percent of overall enrollments in general education, continued in the roughly half of school facilities that they controlled. This situation resulted in serious over-crowding of facilities, and alternatively, the use of non-school buildings and private homes to conduct education. A “parallel” governance structure was gradually established including simple regulations and arrangements for financing the system from within, and from external remittances. Consistent and reliable data on the “parallel” system were not kept, but estimates are that about 20,000 teachers, professors and non-teaching staff supported over 300,000 pupils in roughly 400 primary schools, over 50,000 students in 65 secondary schools and over 10,000 students in 20 university faculties. Enrollment is reported to have declined, particularly at lower levels, throughout the decade due to outward migration and dropouts.

¹ Noel Malcolm (1998) Kosovo: A Short History, Macmillan, page 326.

4. Following the 1991-92 school year, during which little funding was made available to the education system, the informal governance system reportedly succeeded in paying only a nominal US\$11 per month stipend to most teachers and other education sector employees in 1992-93. Between 1994-98, the informal system attempted to pay salaries at minimum rates of between US\$67 to \$89 per month, depending on level and qualification. Although some higher income municipalities reportedly were able to exceed these minimum payments on occasion, nearly all salary payments were made irregularly. As conflict in Kosovo increased over the past 12-18 months, salaries were paid with increasing irregularity. Some teachers are reported not to have been paid for up to 18 months. With the exception of some textbooks, which were predominantly funded from abroad, non-salary recurrent costs, to the extent any were forthcoming, were mostly covered by informal direct parent contributions to schools in cash or in kind.

5. Informal municipality-level tax collection (between 3-5 percent) is said to have provided for about 60-70 percent of education salary expenditure. Contributions collected from abroad accounted for the remainder of education spending, and acted as an equalization fund for municipalities that could not meet the minimum salary payments from local revenue. External funding could not, however, ensure complete equalization, and allocations of external funding were said to be, to some extent, politically motivated. Internally-generated municipality revenues, assigned to education by a municipality financing council, were managed by the municipality education director in cooperation with school directors, as was external funding once it arrived at the municipality level. The cost of supporting the “parallel” education system is estimated at about US\$1.7 million per month, although available financing was frequently less.

The Current Situation

6. **Current Performance and Status.** Despite the remarkable efforts during the past nine years – particularly among teachers – to maintain a functioning education system under extremely difficult conditions, it is inevitable that the quality of education delivered in the classroom has suffered. Because of the lack of student performance information with which to make comparisons (a problem even with the pre-1989 system), it is impossible to say anything definitive about the cost of the past nine years in terms of learning outcomes. Enrollment ratios, thought to be over 90 percent at the primary level prior to 1989, have almost certainly declined substantially over the past decade, particularly among girls.

7. In terms of provision of educational inputs, which say little about system performance, the past nine years and the recent conflict have taken a serious negative toll. As mentioned above, education financing was available only at 10-20 percent of pre-1989 financing levels. Few teachers, professors or administrators – with the important exception perhaps of those living abroad -- have benefited from any organized professional skills upgrading. Even prior to 1989, pre-service teacher training lacked a methodological focus and education administrators were not exposed to modern public sector management skills. In addition, the system as a whole has been isolated for a decade from recent trends and advancements in pedagogy, methodology and education administration and management. Basic textbooks for primary and general secondary education were reported to have been generally available to most students. They were financed through external contributions, but their pedagogical and physical quality is said by teachers to be lacking, and many of these books were destroyed or lost during the recent conflict.

8. The return of students, teachers and school/municipality administrators has reportedly been strong since June, and most schools and the university have organized remedial summer courses in order to catch up with the lost time since education was halted by the conflict in March. To the extent that early numbers are reliable, they show that there is no general teacher

shortage. Student-teacher ratios of 20/1 in primary, 16/1 in secondary, and 14/1 in higher education are even slightly lower than the Western European average at each level. However, these system-wide averages in primary and secondary schools could hide serious over-crowding of facilities balanced by under-utilization of other facilities across or even within municipalities. Shortages of teachers with certain skills, particularly language and computer skills, will also inevitably be a major issue in the coming year.

9. The physical condition of schools in Kosovo presents a serious constraint to re-starting the education system. According to EC/IMG estimates, which continue to be updated, slightly more than half of the approximately 1,000 primary school buildings are in need of repair. Roughly 30-40 percent of primary schools will require light to medium repairs, while roughly 10 percent are seriously damaged. The EC's initial estimate for the costs of repairing/re-building primary schools is about US\$20 million. This estimate does not include the cost of furnishing and re-equipping the schools. The percentage of damage to schools is thought to be about the same for Kosovo's 66 secondary schools. No monetary estimate for repair and re-building of secondary schools has been made. Although the unit cost of secondary reconstruction is higher, the smaller number of secondary schools would probably mean that secondary reconstruction needs would be less than half that of primary. University facilities have not sustained serious damage, but are reported to be in need of re-furnishing and re-equipping. No monetary estimate for higher education reconstruction has been forthcoming from the donors, although university authorities estimate their repair and re-equipping needs at US\$4.9 million. While about 10 percent of school facilities were largely or completely destroyed during the recent conflict, the lack of maintenance during the past decade, and the age of many schools (about 25 percent of school buildings are over 40 years old) are an equal if not greater cause of physical deterioration in most schools.

10. **Initiatives since June:** The most important initiative in education since the ending of the recent conflict and the return of most Kosovar Albanians to Kosovo has been the organization of summer classes at all levels of the system, including the university, in order to catch up with time lost since March. This demonstrated commitment to work without pay is impressive, but most authorities agree that it is unlikely to be sustained into the next school year. The start of the 1999-2000 school year has been delayed until November 8 to give schools and the university time to finish 1998-1999 programs. As teachers and students have returned to the schools, Kosovar Albanian leaders have announced that two months of salaries will be paid at rates of between US\$67-83 per month from existing externally-contributed funds. Although there are some expectations that unpaid back salaries will be paid for the last two school years, it is highly unlikely that financing will be made available from any source to cover this expenditure which would exceed US\$55.6 million if paid in full.

11. The second most important initiative has been the decision of the donor community to fund a recurrent budget, prepared by UNMIK, for the education system during the remainder of 1999 and throughout 2000. The budget is expected to represent an improvement over available funding for education in the "parallel" system, in terms of both salaries and non-salary operating expenditures. But, it will also obviously be constrained by the availability of overall donor funding for a plethora of priority expenditures and the need to stay within realistic expectations for revenue generation in Kosovo in the medium term (see budget section below). In order to avoid teacher strikes, school closings and possible civil unrest, it will be particularly crucial, given expectations, for the donor community to follow through on its commitment to make funding available in a timely and consistent manner at the beginning of the upcoming school year.

12. In terms of what will be taught in the system, Kosovar Albanian authorities and UNMIK have decided to use the existing curriculum that was in use under the “parallel” system for the school year 1999-2000-- although there is consensus that this curriculum needs to be replaced as soon as possible with a more up-to-date framework of subjects and performance standards. Likewise, a decision has been made to re-print existing textbooks, at least for core primary and secondary subjects, for use during the 1999-2000 school year, pending a curriculum and textbook review in the coming 1-2 years. Special donor funding has already been mobilized for this initiative.

13. Finally, a major, if inevitably uncoordinated effort has currently been under way by KFOR and numerous donors and NGOs to repair, or at least winterize, as many schools as possible prior to the beginning of the coming school year and the onset of winter. Although little reliable information is available now, this effort is likely to be largely successful in most areas. However, particularly in cases where extensive civil works or complete re-building of schools are needed, some schools will not be operational during the school year and alternative solutions will have to be found, as in the previous “parallel” system. The lack of wood and fuel for heating is also expected to be a serious impediment to education, as well as a lack of basic school furniture in many classrooms, except to the extent that donors can ensure supplies.

14. **Institutional Situation:** The current institutional situation in education is marked by competing claims to authority and responsibility for creating a Ministry of Education between the former government in exile and the KLA-backed provisional government. It will be difficult for major donors to support any Kosovar Albanian-led policy or development initiatives at the central level until lines of authority for education are drawn. The majority of donors are currently dealing directly with the UNMIK Education Department, which has only very limited implementation capacity to date. Without significant additional staff, the UNMIK Education Department will find it exceedingly difficult to oversee programs or enforce interim policy decisions. A Joint Civil Committee for Education has been created under UNMIK’s Education Department. The JCCE is made up of four representatives from the Albanian language system, two from the Serb language system, and representatives from UNESCO, KFOR and UNICEF. To date, the JCCE has performed a consultative, but not a decision-making function. The UNMIK Education Department has been investigating the potential for inviting technical staff to join working groups to learn and begin thinking about strategy alternatives in key areas, such as education finance and governance, curriculum, assessments, textbooks, and secondary and higher education reform.

15. Although there are undoubtedly some un-resolved problems at the municipality level, leadership responsibility and lines of authority are generally not thought to be a serious problem within the Kosovar Albanian community. The formation or continuation of parallel institutions between Serb Kosovar and Kosovar Albanian municipal officials, however, presents a serious problem for which the immediate solution-- as in parts of the Federation of Bosnia and Herzegovina-- may be in the short-term to accept parallel structures in order to ensure provision of education services, while providing incentives for cooperation -- for example, in terms of co-managing funding and working together on highly technical issues.

16. **Aid Coordination:** To reduce the inevitably uncoordinated nature of numerous donor interventions for education in Kosovo, the UNMIK Education Department should pay particular attention to aid coordination, prioritization of donor activities, and dissemination of information through periodic donor update reporting. All donor investments should be approved by UNMIK, and dedicated staff should be hired to monitor and report on donor activities.

B. SECTOR STRATEGY AND PRIORITIES

Development Policy

17. In view of the highly uncertain political and institutional situation, and the long time isolation of Kosovo's professional educators from external advancements in their profession, it is not realistic to expect authorities in Kosovo to develop a detailed, realistic and appropriate education strategy or policies in the short-term. The development of a locally prepared education strategy, which addresses the sector across its component parts (levels, inputs, performance, etc) and in its economic and social context, should, in fact, be seen as a medium-term (2-3 year) objective. However, despite the lack of a comprehensive education strategy, the system's obvious reconstruction needs do permit the development of a short-term investment program designed to ensure a minimum level of educational delivery in the 1999-2000 and 2000-2001 school years.

18. In terms of supporting strategy development, perhaps the most effective thing that donors can do is to provide opportunities to local educators and education authorities in terms of exposure to external innovations, technical assistance, training and pilots (learning by doing), which will serve to mitigate the isolated nature of the system over the past 9-10 years. An education technical issues council or working group should be set up to supplement the work of the JCCE. This group of working level professionals would be expected to serve as a focal point for debate, knowledge accumulation, and participatory consensus building in the sector. This group would be expected to represent various levels and viewpoints (public/private, unions, administrators, pedagogues, etc), and would eventually be expected to provide a forum for policy dialogue and strategy development in the sector.

19. It is important to note that, while there is a tendency to focus on the uncertain education governance situation and the immediate effects of the recent conflict (damaged facilities and unpaid teachers), the education system in Kosovo needs to begin a transition that has been underway in many of its central and eastern European neighbors for the past 7-8 years. Education and political authorities in Kosovo and the donor community should be focused, not on rebuilding the previous system, but on taking advantage of the opportunity presented to build a modern and responsive educational system that is compatible with a new economic environment, and with European performance and institutional standards.

20. While comprehensive, locally-driven strategy and policy development will take time to evolve, there are a number of things that can be said about what sort of objectives an education strategy for Kosovo would be expected to address.

Education Governance and Financing

21. The current unsettled situation in education presents an important opportunity to establish modern mechanisms and incentives that will serve to enhance quality, efficiency, and equity in the system. As a general western trend, the key to establishing an efficient distribution of responsibilities and functions in education is twofold: first, to allocate to the center the authority for policy/strategy formulation and for ensuring equity of access (redistribution to disadvantaged areas) and the quality and consistency of educational programs; and, second, to ensure that lower levels are given the responsibility and authority (including budget and expenditure authority) to implement programs flexibly and creatively within established norms. In fact, the education system in the SFRY, in contrast to its central and eastern European neighbors, was an early and interesting example of just such a division of authority and responsibility in education. This

tradition of decentralization in education was continued by the Kosovar Albanians in the operation of their “parallel” education system over the past nine years, as municipality education authorities were given significant discretion for managing both locally-generated and centrally-provided resources for education. This authority entailed mainly assigning and re-allocating personnel (salaries were centrally established), but also involved working with informal cash and in-kind contributions from parents.

22. Given western trends and local traditions for education decentralization, a priority for authorities in Kosovo and the donor community should be to continue a policy of decentralization to ensure the authority of municipal officials to manage the majority of resources for education. However, unlike in FRY, where locally-generated revenue was kept at the municipal level to fund education, authorities in Kosovo should consider various alternatives including a system of fiscal devolution for education funding in which central revenue is devolved to local education authorities on an equitable, per student basis. The design of such a system of fiscal devolution for education in Kosovo would include two crucial elements:

- 1) Once the relative priority for education in terms of overall budget allocation – in competition with other sectors and priorities -- has been determined at the center, the distribution of resources for education to the municipalities would be carried out in the form of block grants on the basis of a per student budget formula. Such a formula-approach to education funding – common in Western Europe and North America, and recently adopted in Hungary, Poland and the Czech Republic -- would help ensure equity (all children in Kosovo would be entitled to an equal level of funding), and would provide a powerful incentive for municipality officials to manage education resources more efficiently. The formula can be adapted to take into account existing disparities (separate urban and rural budgeting norms, for example), and to allow additional spending for programs in low performance areas. A centrally-mandated public pay scale for teachers and other employees in education could be maintained under such an arrangement. The introduction of per student funding would also contribute greatly to transparency in terms of allocation of resources across ethnic groups.
- 2) despite the tradition of local management and financing councils, priority would have to be given to supporting municipality governance structures to develop their public administration skills, and for re-defining the role of local school boards and parent associations -- which are mandated without much description in informal Kosovar Albanian legislation. Local school boards, in particular, should be expected to play an important role in ensuring accountability in the definition of local priorities and the expenditure of funds to achieve those priorities.

The central ministry’s role in ensuring educational standards and consistency within a fiscally devolved system is discussed below in the curriculum and assessments section.

23. As a last point on education governance, a high priority should be given to helping authorities at all levels ensure the availability of reliable administrative, financial and performance information. This is a pre-requisite for beginning a productive dialogue on education reform, and for facilitating strategy and policy development. The development of per student formulas and a focus (see section on curriculum and assessment below) on measuring learning outcomes will go a long way toward helping to measure inputs and outcomes in the system. Helping to create capacity for producing and using management information at the central, municipality and school levels should be a priority for the governance reform strategy, which should be supported as a priority, by the donor community.

Higher Education Governance and Finance

24. Unlike modern, integrated universities in Western Europe and North America, the University of Kosovo operates as a loose association of faculties, academies, colleges and institutions, each with a legally autonomous status and management structure. This dispersal of authority in what should be a single institution has led to a redundancy of programs, personnel, and facilities across faculties. This diverts resources from improving the quality of teaching and learning. The weakness of the university rectorate also hinders an effective prioritization of programs in the face of a changing economic and social environment, and allows autonomous faculties to resist systemic reforms aimed at investing efficiency gains in improving the quality of programs. As the university is re-established and new legislation is drafted over the coming months/years, authorities in Kosovo should not miss the opportunity to make their university compatible with European standards in university governance and management. Along with new legislation, there is a need for a strategy aimed at developing academic and institutional accreditation within Europe in the medium-term. Authorities should consider establishing a representative university council or working group to discuss needed reforms with donors, and to begin the process of preparing new legislation and an institutional development strategy.

25. Per student funding formulas for various programs should also be developed for higher education as a way to instill transparency of funding, and provide incentives for increased efficiency. The potential for a gradual institution of fee charges for various high demand programs should also be closely examined as a way to focus more resources on qualitative improvement, in combination with the development of student loan schemes and fellowships targeted on the basis of need. Cost recovery should be re-instituted as soon as possible – nominal fees of around US\$39 per student were collected during the “parallel” system -- in terms of requiring increased student contributions to previously subsidized dormitories, food and transport costs.

26. Because governance and finance issues in higher education are fundamentally important to ensuring the long term pay-off of investments in the university, major donor investment in the university – including the EC’s Tempus program – should be aimed at supporting governance and finance reforms prior to, or at least concurrent with, committing direct investments to improving the quality of programs in individual faculties. The key for donors is not to allow direct investments to reinforce the inefficiency and redundancy of the current governance structures. The most effective action that donors could take immediately in this area would be to assign a qualified consultant to UNMIK Civil Administration who would be charged with helping to organize the council or working group mentioned above. The aim would be to upgrade their skills, knowledge and understanding of higher education trends and reforms in Western Europe and in neighboring countries in Central and Eastern Europe which have already begun higher education reform programs. This would be done in preparation for designing a coherent higher education reform strategy. Apart from support for university restructuring, specific higher education programs, which respond to particular development needs or skills shortages – such as the development of programs for medical, business administration and public administration programs – should be a first priority for donor financing. Support could be provided directly to the university or through creation of a Re-Training Fund, from which the university would have access to resources in competition with other training providers.

Curriculum and Assessments

27. There is an awareness among leading professional educators in Kosovo that educational programs at all levels are characterized by a dense and ambitious body of knowledge to be

learned, leaving little flexibility to focus on thinking and learning skills, or to dealing with children with varying capabilities. In order to make the education system responsive to changes in the skill needs of the labor market, reforms will be needed not only in what is learned in school, but in how it is learned. Rather than focusing on a traditional redefinition of precise curriculum content and syllabi, course by course and level by level, local authorities should take time to review recent innovations in western European education systems which focus on defining learning objectives and performance standards in the context of a coherent curriculum framework. Closely tied to this focus on performance standards is the need to develop a capacity-- currently non-existent in Kosovo -- to measure student performance in a standardized manner. The availability of student performance or "outcome" information helps ensure the accountability among education authorities to the public they serve. This is key to allowing education authorities at all levels – school, municipality, and center – to identify problem areas, and to focus programs and resources on improving student and school performance.

28. In keeping with past tradition in the SFRY and recent western trends in education, the authority for developing and monitoring a curriculum framework and modern learning standards should be placed at the center. However, in such a small area as Kosovo, the process of change should be as consultative as possible. Agreement on an institutional mechanism and process for beginning this fundamental effort should be a priority for the coming year, and donors should make every effort to expose leading stakeholders throughout the system to technical and process innovations in neighboring countries and in Western Europe. It will obviously be important to ensure maximum flexibility in any curriculum framework to accommodate the desire on the part of minority groups to define and control their learning process at decentralized levels. As is the hope in neighboring Bosnia and Herzegovina, part of the answer to ensuring standards in the context of a non-cooperative environment across different groups could be a focus on developing a student assessment capacity, which could be carried out on an independent, professional basis. It is too early to pre-judge the appropriate institutional arrangement for assessments, but developing such a capacity, to cover all children in Kosovo, should be a priority for local authorities and for donor investment.

Textbooks

29. The eventual development of a modern curriculum framework for Kosovo, together with changes in information technology, will obviously determine the number and types of textbooks and other educational materials that will be needed in the medium-term. It goes without saying that the hundreds of textbooks currently prescribed for the system will no longer be justified or sustainable once the structure and orientation of programs have been reformed. The decision to use existing curricula and re-print existing books for the beginning of the coming school year takes the pressure off the need to develop new books that may or may not be appropriate for curriculum changes in the future. Given the myriad priorities and urgent reform needs in education, decisions on privatizing textbook production and re-organizing textbook selection and financing can be delayed until curriculum reform efforts are underway.

Teaching and Learning

30. Most teachers in Kosovo have been isolated from professional innovations and professional skills upgrading over the past nine years. A further constraint in the system is that pre-service teacher training faculties and academies in Kosovo and the SFRY did not traditionally emphasize child-centered or inter-active teaching methodologies, nor the need to use student evaluations to improve their effectiveness. There is, therefore, complete agreement among education authorities in Kosovo that the top priority in terms of having an immediate positive

impact, should be to upgrade the teaching skills of nearly all the estimated 24,000 primary school teachers and 4,500 secondary teachers currently serving the system. Local authorities and donors should balance support between the need to redefine pre-service teacher training curriculum and to restructure delivery mechanisms for in-service training (both medium- to long-term objectives which should start soon) with the need to provide at least some remedial training to existing teachers with a degree of urgency over the next year or two. NGOs and organizations, such as UNICEF and the local Open Society Institute, should play a major role in helping to organize both medium-term teacher training reform, and in offering urgent skills training to teachers in the short-term. A number of interesting and successful pilot or experimental school projects are ongoing throughout the region (particularly in the Former Yugoslav Republic of Macedonia, Albania and Bosnia and Herzegovina), and these interventions could offer a starting point for authorities in Kosovo to learn about innovations and opportunities.

Secondary Technical/Vocational Education and Adult Training

31. Approximately 70 percent of secondary students are estimated to be enrolled in specialized technical and vocational programs throughout Kosovo. Degree courses are offered for such specialties as waiters, cooks, shop assistants, nurses and tailors. However, due to the constraints of the “parallel” system and the recent destruction of facilities and equipment and loss of books and materials, many specialized schools will undoubtedly succeed in organizing only general core subjects and theory-based courses in the coming school year. When operating normally, specialized technical and vocational programs are often expensive to operate – due to low student/teacher ratios and equipment needs. Graduates are trained in narrow, occupational specializations for which there is currently questionable labor market demand.

32. As currently designed, the secondary system in Kosovo is out of alignment with the emerging market economy’s need for broad-based skills, labor flexibility and continuous learning. It is crucially important for donors not to rush into the re-establishment of the current secondary system until local authorities have developed a strategy for secondary reform. Focus should then be put on the medium-term objective of developing new broad-based programs, and on an extensive re-training program for the existing secondary teaching force.

33. A reform of secondary technical/vocational education will also necessitate commensurate reforms in the field of adult training and two-year higher education technical/professional programs. The goals are to develop a network of training suppliers (public university, private-for-profit, semi-public, NGOs, etc.), to bring social and private sector partners into the governance of adult training, to complement government funding with cost recovery, and to facilitate the availability of labor market information. In this context, there is an urgent need to provide remedial training for specific skills such as business/enterprise management, and various technical and engineering skills needed to ensure an effective operation of public sector resources and utilities.

34. As with higher education reform above, the most effective action donors could take immediately to promote strategy development is to assign an experienced consultant to UNMIK, who would be responsible for working with a representative working group of secondary education authorities to upgrade their skills, knowledge and understanding of issues in this crucial area. An agency such as the European Training Foundation, which has extensive experience in neighboring countries, would be ideally suited to play such a role.

C. FINANCING NEEDS

Recurrent Budget Needs 1999-2000

35. The UNMIK Education Department has prepared provisional recurrent budgets (see annex table) for 1999 and 2000, which will be funded through donor contributions. The most important decisions were the establishment of interim salaries and a non-salary spending contribution adequate to keep teachers in the schools and to allow minimal school operating costs, while being sustainable in terms of expectations of donor contributions in the short-term and reasonable revenue generation prospects in the medium-term. There remains some uncertainty about the final number of education sector personnel who may be placed on the UNMIK payroll for 1999. However, the average student-teacher ratios implied by the current figures are within historical limits. Final student-teacher numbers will be verified by municipality prior to the execution of salary payments.

- **Salaries.** Although teachers in Kosovo have expectations, following nine years of hardship, of returning to pre-1989 salary rates, it is clear from GDP estimates that the Kosovo economy will not support relative pre-1989 wage rates in the short- to medium-term. The setting of interim 1999 salary rates was, therefore, calculated to provide some improvement in salary rates over what was paid irregularly in the “parallel” system, while attempting to ensure that initial salaries are sustainable once donor contributions to recurrent financing are discontinued. Initial average net salaries of US\$100 for primary teachers, US\$139 for secondary teachers and US\$222 for university professors are, in fact, only slightly lower than current wage rates in the Former Yugoslav Republic of Macedonia, and in both entities of Bosnia and Herzegovina. The relative salary scale which was used in FYR and the “parallel” education system for various levels and qualifications has been maintained. Gross salaries will be calculated for 2000 and beyond and, depending on economic recovery and revenue growth, net pay rates are expected to be at least maintained in 2000 and beyond. Donor experience in Bosnia and Herzegovina has shown that wage rates have recovered in terms of regional norms within three years.
- **Non-Salary Budgets/Expenditure.** Non-salary spending has been calculated as 20 percent of the overall education wage rate, which translates into non-salary per student spending of about US\$17 per student in primary, US\$28 per student in secondary, and US\$50 per student in higher education. A typical eight room primary school of approximately 320 students would be entitled to about US\$12,500 in expenditure for goods and services. Expenditure categories will be limited to pedagogic materials (books, paper, and other learning materials), heat and other utilities costs, replacement furniture and light equipment (no single item over US\$111 or single contract over US\$556 without special authorization), maintenance costs (cleaning supplies, winterization, small works less than US\$1111 per contract without special authorization), and administration costs (record books, office supplies). Salary supplements and major civil works will not be permitted, and school furniture and equipment such as computers and photocopiers will be approved by UNMIK only on an exceptional basis. Student transfers or subsidies would not be allowed except through prior authorization by UNMIK. UNMIK intends to organize auditing of selected municipalities/schools to ensure compliance, and the auditing function should be announced publicly in advance.
- **Capital Budgets/Expenditure.** School reconstruction, re-equipment and re-furnishing needs are expected to be covered in their entirety by donors (see Priority Investment Plan below). To the extent they are not in an urgent time frame, minor winterization and

furnishing costs can be covered by schools from their goods and services budgets. UNMIK should guide and track capital expenditure on the part of the donors, and provide up to date information on implementation and achievement as measured against reconstruction goals. As mentioned above, existing textbooks will be re-printed for the 1999-2000 school year as an interim measure with donor financing already obtained.

36. The recurrent budget is presented below in per student terms. The figures represent on average of about 40 percent of comparable per student spending numbers for Bosnia and Herzegovina and the Former Yugoslav Republic of Macedonia, reflecting, in part, the fact that salaries in Kosovo will be paid net of taxes in 1999. It is recommended that the non-salary component be allocated to municipalities/schools on a per student basis. Per student allocations of non-salary funding would serve to push decisions on funding priorities to the municipalities, which have a tradition, both under FRY and during the “parallel” system, of decision-making at that level. A per student allocation would also serve to ensure equity across the municipalities and schools, as well as different groups. It would also provide a premium to overcrowded facilities (those with high student-teacher ratios). Eventually, the allocation of all municipality level education expenditure on a per student basis could provide a powerful incentive for using the most expensive educational inputs (teachers and facilities) more efficiently.

Table 1: Per Student Recurrent Spending (in US dollars)

	Students	US\$ /Student
Primary		
Total budget per student	281,000	87
Non-salary budget per student		14
Secondary		
Total budget per student	78,901	119
Non-salary budget per student		20
University		
Total budget per student	33,000	211
Non-salary budget per student		35

Capital and Other Non-Recurrent Development Expenditure 1999-2004

37. Detailed surveys of capital/reconstruction requirements will be completed by the European Commission/IMG in December 1999. A preliminary estimate of the costs of a three to five year priority program of capital renewal, upgrading personnel skills and strengthening local institutions and supporting capacity development is summarized in the table below. The cost of repairing and re-equipping conflict-damaged, old and poorly maintained primary schools and higher education institutions are based on estimates provided through a preliminary EC/IMG survey carried out in July. These figures need to be updated as new information becomes available. Secondary education reconstruction needs have been estimated based on experience in Bosnia and Herzegovina. The University of Kosovo provided the estimate for university physical rehabilitation needs. In the outer years of the investment program, more and more emphasis will have to be given to prioritized investment programming for facilities and equipment (as part of a school mapping data base) in the context of inevitably diminishing resources, facilities consolidation and more difficult investment trade-offs.

38. Estimates for textbooks represent funding needed to re-print existing books on an emergency basis, as well as funding needed to procure new published books to respond to new curricula in outer years. The amounts allocated for capacity building and strategy development

reflect the capacity of a new administrative structure to absorb local and external technical assistance and training, and the need for phasing of priority reforms. Emergency re-training funds for teachers and for certain needed skills (managerial, technical, professional) that are lacking or need to be updated, is also based on experience with re-training funds in Bosnia and Herzegovina and elsewhere in the region.

39. Estimates of funding requirements will need to be confirmed and updated as more information is forthcoming in the coming months. Given financing constraints and competing priorities, it also represents a highly prioritized investment program that is designed to: (a) ensure a minimum acceptable standard of education delivery in Kosovo in the medium term; and (b) be implementable in terms of the capacity of donors and local authorities to manage a large inflow of external funding in a complex political and institutional environment.

40. Donors should consider addressing the re-training needs by supporting the creation of a Re-Training Fund to be managed by a tri-partite board made up of government, business, education and union leaders. Such a board could be established initially by UNMIK on the basis of local consultations. The next step would be to finance a small professional secretariat (an NGO or donor could provide a mix of local and external consultants), which would take the lead in defining, in consultation with the board, criteria for selecting and funding re-training proposals. The criteria would give priority to management and technical skills where there are current shortages, and to remedial skills training for youth whose education was disrupted during the recent conflict. On the basis of published criteria, a network of suppliers would be expected to submit funding requests-- including industry and enterprises, secondary schools, university faculties, employment offices, unions, NGOs-- to bilateral and multilateral donors, and to private sector training providers (private suppliers would probably focus initially on languages and computer skills). Re-training contracts for all types of training can be simplified by basing them on average unit costs per trainee. A minimum level of job placement can be mandated following training and/or financial incentives that can be included in the contracts to reward a high rate of job placement. Variations of this mechanism have been used successfully throughout Central and Eastern Europe during the past decade to promote skills development and re-structure adult training.

41. Based on the strategy presented above, and in view of implementation capacity on the ground in Kosovo (both on the part of donors and local authorities), capital, recurrent and development funding needs in the short and medium-term can be summarized as follows:

**Table 2: External Financing Requirements for the Education Sector
(in millions of US dollars)**

Activity	First Phase (until December 2000)			Second Phase (2001-2003)	Total
	Until March 2000	April to Dec. 2000	Total		
INVESTMENTS					
Primary schools reconstruction and refurbishing	4.0	17.0	21.0	14.0	35.0
Secondary schools reconstruction and re-equipping	1.0	5.0	6.0	7.0	13.0
Repair and re-equipping of University facilities	0.0	4.0	4.0	1.0	5.0
Printing of existing core titles in 1999/2000	0.0	2.5	2.5	0.0	2.5
Publishing of new core books in 2001-2003	0.0	0.0	0.0	5.0	5.0
Emergency Re-training Funds	5.0	8.0	13.0	7.0	20.0
Subtotal	10.0	36.5	46.5	34.0	80.5
TECHNICAL ASSISTANCE	1.0	1.5	2.5	2.0	4.5
TOTAL²	11.0	38.0	49.0	36.0	85.0

² In addition, about US\$206 million will have to be funded through the budget for operating expenditures in the sector.

ANNEX VII: HEALTH

A. SECTOR DESCRIPTION

Description of the Health Sector until 1989

1. The health system was organized with financing and planning functions at the provincial level in Prishtina. Inpatient services operated through one tertiary hospital (Prishtina), five other district general hospitals, a specialist TB hospital, a rehabilitation unit, and a spa/sanatorium. Primary health care was delivered through larger clinics, “health houses”, in 29 municipalities overseeing a network of dispensaries (small clinics) and pharmacies. Municipal governments did not have ownership or responsibility for management of health care or health care financing. Municipalities were responsible for some public health functions such as sanitation inspection, and some licensing functions. Some tertiary cases and mental health patients were referred outside of Kosovo to hospitals elsewhere in FRY. This network of health care providers remains in place in 1999. In this period, hospitals and other health provider organizations selected their boards and directors independently, and a self-management committee in each institution made decisions on hiring employees, though the process often lacked transparency. Private medical practice and private hospitals were not permitted prior to 1990.

2. As in other parts of SFRY and most Central European countries, the health care system was, and still is, characterized by high reliance on specialists, high referral rates from general practitioners to specialists working in primary health care and in hospitals, and use of medicines and technology often without reference to evidence of effectiveness. General practitioners were not provided with, or expected to possess adequate training for modern family medicine. Primary health care service delivery was divided among different sub-specialties based on age, sex, disease type, and location, in a fragmented and inefficient way. Of 1816 medical practitioners in 1989, 643 were specialists, and a further 387 were residents in specialist training positions. Only 705 worked as general practitioners. Of 392 dentists, 131 were specialists and 77 were residents in specialist training. There were some 5750 nurses and 3500 non-medical support staff, bringing total employees in the health sector to around 12,000. Most nurses had only secondary school-level vocational qualifications. Post-secondary school nursing education was and remains unavailable within Kosovo.

3. The Kosovo health system was financed through a Health Insurance Fund organized as a “self-managing community of interest” (SIZ) at the central level of the province, and through 29 “elementary units” (OZs), which were municipal branches of the SIZ at the community level. This health insurance system provided insurance for health care and a range of cash benefits (for sick leave, disability, funeral benefits, eyeglasses, orthopedic devices, etc.) to those who paid insurance contributions and to their families. Health insurance revenues were derived from compulsory contributions from employers and employees, calculated at 9 percent of gross salaries. This source accounted for 80 percent of Health Insurance Fund revenue. The pension fund contributed 14 percent of pension income for pensioners; other social funds also contributed. Farmers and small businesses contributed 20 percent of farm income in theory, but in practice, collection was ineffective. As many Kosovars worked abroad, around US\$7 million was contributed from Health Insurance Funds in foreign countries on their behalf in 1989, to cover family members living in Kosovo. In addition, 8.5 percent of revenue (US\$5.8 million in 1989) for health care came from a federal solidarity fund.

4. The OZs paid providers according to a modified fee-for-service (points) system. Point values and prices were determined centrally in Prishtine. However, the prices paid were adjusted periodically through each year to balance revenue and expenditure. There did not appear to be any form of utilization control. OZs also assessed claims by local insurees for cash benefits and paid these. The SIZ was responsible for deciding when the Health Insurance Fund would pay for treatment outside of Kosovo for patients requiring tertiary care or mental health services not available within the province. Around 12 percent of revenues were spent on treatment abroad, mainly in Serbia and in the Former Yugoslav Republic of Macedonia. The regulatory and finance system did not create incentives for efficiency: the price system derived from norms for the number of beds, equipment, staff ratios, and building size. The financing system also encouraged higher numbers of hospital bed days, and hence longer than average length of stay. Relative prices were based on planning norms and absolute prices were not market-based, but rather simply adjusted according to available funds. In these circumstances, as the real payments for services declined, informal co-payments for services emerged as a supplementary source of finance.

5. By 1989, the health system was already in financial deficit. Expenditure exceeded revenue by 24.5 percent. Public revenue collected in the same year was US\$68.9 million, while expenditures amounted to US\$89.8 million (about US\$55 per capita, or around 4-4.6 percent of Kosovo GDP, which was around half that in Serbia). A number of structural, legal, financial and political issues needed to be resolved before a sustainable health finance system could be established.

Recent History: 1989 - March 1999

6. Over the period 1990-1992, the management of the health system was centralized. The Belgrade Ministry of Health was responsible for policy in Kosovo, and a branch of the Ministry in Prishtine represented Belgrade. The Ministry of Health appointed boards and directors of health care institutions. A central Health Insurance Fund in Belgrade took responsibility for health finance in Kosovo, Serbia and Vojvodina, with 30 regional branch offices throughout the Republic. There were five branches in Kosovo based in Prishtine, Prizreni, Gjilani, Peja, and Mitrovica. Health contributions were collected at this regional level. The official policy was that 70 percent of revenues were retained at this level, and 30 percent remitted to a solidarity/equalization fund in Belgrade. Local perceptions are, however, that almost all revenue was remitted to Belgrade, and that redistribution to the regional level was non-transparent. At the same time, the prohibition on private medical practice was removed.

7. Most Kosovar Albanians were dismissed from management and senior positions in the health system, as in other public services, in 1990-1992. Many opened private medical practices. Many Kosovar Albanians had limited access to coverage under the centralized health insurance system. For example, more than 50 percent of Albanians did not have a social insurance card, needed for Health Insurance Fund coverage. A parallel charitable primary health care system developed to provide basic health services free of charge to those who could not afford private medical care and did not have a "social card" was organized through the Mother Theresa Society. The Mother Theresa Society established 96 clinics throughout Kosovo, often in remote village areas with predominantly Kosovar Albanian populations. Mother Theresa Society staff worked voluntarily in these clinics and other resources were financed by a parallel tax system. It appears that in severe and urgent cases requiring hospitalization, many Kosovar Albanians continued to be treated in the public hospital system.

8. Private practice and informal out-of-pocket payments became a larger source of income for medical personnel (estimated by some to exceed official public sector income on average), particularly for specialists, during the 1990s. Real decline in public sector salaries, and delays in salary payment in recent years contributed to this situation.

9. Kosovar Albanians organized a system of parallel medical education, as they were no longer able to obtain medical education in their own language in this period. Over 700 doctors and 1200 nurses have graduated from this system. There are concerns about whether this system was able to provide an adequate range of clinical training opportunities to achieve acceptable quality (for example, due to limitations on opportunity to obtain hospital experience), and about the lack of formal recognition of qualifications earned through this system.

The Current Situation

10. **Current Performance and Status.** During the conflict, Mother Theresa Society facilities sustained the worst damage, with only 10-15 percent remaining operational, mainly in the cities. The hospitals and most health houses are intact. Damage has occurred mainly in remote dispensaries and small clinics. A preliminary EC/IMG damage assessment (July 1999) estimates costs of 4 million Euro (US\$3.8 million) for repairs of conflict damage, and provision of equipment to dispensaries and health houses. The building used jointly by the Health Insurance Fund, Social Welfare Agency and Pension Fund in Prishtine was damaged by bombing.

11. The effects of the conflict added to underlying problems due to a period of ten or more years of neglect, poor policy and weak management. There has been chronic under-investment in maintenance of physical infrastructure and equipment, and in staff development. The general impression, in the absence of thorough assessment, is that much of the equipment installed in the hospitals is obsolete, out of order due to poor maintenance, unused due to lack of consumables, or under-utilized due to lack of personnel. The Health Insurance Fund has estimated that almost 80 percent of equipment should be progressively replaced.

12. Many health professionals who worked in Mother Theresa Society clinics have now abandoned this system to seek employment and specialist training positions in hospitals. The prevailing view appears to be that there is no more need to maintain a parallel system. As a result, this means of providing health care for the poor and in rural areas is now in decline. Since the conflict, most health institution managers and senior doctors, who were Serb Kosovars, have left their posts. Kosovar Albanians who were expelled from positions after 1989 have returned to the system, reclaiming their old jobs. Medical staff who graduated from the parallel system also claim a right to positions in hospitals that would enable them to complete an "intern year" of supervised practice, and then obtain registration.

13. The combined effect of these trends is that doctors have now moved from primary care to the hospitals, hoping to work or train as specialists, over-burdening the hospitals and the system of specialist clinical training, while primary health care facilities, particularly in remote areas, are deprived of staff. The distribution of health care facilities and of health professionals across Kosovo was already inefficient and inequitable, with a relative concentration in Prishtine, alongside scarcity of primary health care facilities and doctors in many rural areas. Large segments of the population, especially the rural poor, have limited access to modern health services.

14. There is scope for improved efficiency in health services. Average length of stay is very high at 12.5 days, and occupancy rates are rather low at 75 percent. Larger hospitals are

organized in separate clinics, with duplication of functions such as pharmacy, diagnostics, and procurement across these. Primary health care facilities are fragmented into too many small dispensaries, unable to offer 24-hour care or to achieve economies of scale in use of equipment and infrastructure. The ambulance system does not cover non-urban areas. Many patients bypass the general practitioner to see a specialist in a health house or in a hospital. Mental health services, TB treatment and services for people with disabilities continue to operate on a basis that relies too heavily on inpatient care, and need to be modernized to shift services of a community-based model.

15. The level of clinical skills among health professionals is a concern. Kosovar Albanians educated in the parallel system and those working in the Mother Theresa Society system or private sector have had little access to facilities for updating knowledge of changes in medical technology and evidence of effective practice for the past 10 years. There is no specialist training program in family medicine. Post-secondary school nursing education is not available in Kosovo, though a small number have graduated from programs in other countries. Some professions allied to medicine (such as physiotherapy) appear to be in short supply.

16. Provision of safe drinking water and sewerage disposal was already a problem prior to the recent conflict, and is likely to be worse now. Rural wells commonly suffer fecal contamination from pit latrines. Sewage from urban areas is discharged untreated into rivers. Chemical contamination may be an issue in industrial and mining areas. Immunization coverage is extremely low --below 50 percent completion of extended program of immunization.

17. **Institutional Situation.** *Public sector hospitals and clinics:* Since 1989, health institution management positions have been occupied exclusively by Serb Kosovars. As these staff have left since the crisis, new managers, often local political party appointees, have occupied these positions. Although elections were used to fill some positions, in general, these new staff were not appointed on the basis of merit, they lack management skills and there are reports that some lack health sector experience also (particularly at municipal level). The formal governance structure for managing and overseeing hospitals and primary health care has broken down. Some parallel features of organization in Mitrovica hospital have emerged, where some 600 Serb Kosovar staff and 300 Kosovar Albanian staff are still working in the same institution. Each staff group tends to function separately, serving its own ethnic community. Serb Kosovar staff continue to receive some salary payments from Belgrade.

18. The *Health Insurance Fund* has essentially collapsed. It is collecting no revenue, has no funds on hand to disburse for cash benefits or provider payments, and the donor and NGO processes for assistance have bypassed the Health Insurance Fund. Prior to the crisis, there were around 400 staff in the Fund. There are now 28 staff in the Prishtine office, around 10-15 in another four district offices, and 3-8 in 29 municipal offices. A number of these staff are pre-1989 Health Insurance Fund staff who have returned to their posts. There is no private insurance.

19. The *Institute of Public Health* is relatively better placed to resume its functions of health protection and disease control, including testing and surveillance-- though equipment and supplies are needed, and staff skills need to be upgraded and modernized. There is a central IPH and five district IPHs.

20. WHO has established a group of policy, planning and administrative staff in Prishtine to assist UNMIK Pillar II in carrying out the functions of an interim Ministry of Health. A Joint Civil Commission (Health), with representatives of Kosovar Albanian and Serb Kosovar communities advises UNMIK on policy decisions. Several task forces with joint WHO/Kosovar

membership support the work program. In the near future, Kosovar counterparts will be appointed to work alongside each of the UNMIK Pillar II health personnel, and the WHO policy and planning personnel. International staff have been appointed to manage the six general hospitals, and an UNMIK appointee will act as district health services manager, assisted by a WHO appointee, in each of the five districts. In addition, a lead NGO has been nominated in each of the five districts of Kosovo, to coordinate activity and liaise with WHO.

21. **Initiatives Taken Since June.** Over 100 donor organizations and NGOs have entered the health scene in Kosovo since the end of the conflict, and a wide array of disparate initiatives are underway. WHO, under the auspices of UNMIK Pillar II, has produced Interim Policy Guidelines for the Future Development of Health Services in Kosovo. This document has been revised with input from a range of donor and NGOs and with the participation of Kosovar health system representatives. It has been approved by the Joint Civil Commission (Health) of UNMIK, and issued in September.

22. During August, a donor-driven proposal got underway to pay stipends to public health system employees. The payments have been described as “stipends” rather than “salary”, with the intention that these are simply temporary humanitarian support, and do not entail recognition of rights of employment in a particular post or any commitment regarding future salary scales. Donors have pledged funds to pay for pharmaceuticals for primary health care for the next six months, and for hospital drugs for some, but not all, hospitals. Humanitarian supply has bridged the gap, while Pharmaciens Sans Frontieres and other organizations have put in place essential drugs lists, and have begun procurement and distribution. There are gaps in resources for non-salary, non-drug operating costs. Interim arrangements for regulating import and manufacture of pharmaceuticals are being put in place. Guidelines for drug donations have been disseminated to mitigate risks of expired or therapeutically useless drug donations.

23. Some initiatives to equip and refurbish hospitals are already underway. However, there are worrying signs that investment is already occurring which is in conflict with the WHO policy guidelines for rationalizing the health sector, and adopting priorities to meet urgent needs for basic services first. Hospital capacity has already been expanded in at least one location, and distribution of donated equipment is creating “feast” and “famine” disparities.

B. SECTORAL PRIORITIES FOR RECOVERY

Priorities for Support and Reconstruction over the Next 12 - 18 Months

24. **Recurrent Costs.** Support for the recurrent costs of operating health services is the highest priority: paying basic salaries to personnel, supplying drugs, and meeting other essential operating costs of hospitals and primary health care facilities. Donor support has been received to cover a first round of stipends payments to health personnel, and for some but not all essential pharmaceuticals for the next few months. Un-hypothecated donor support is needed to meet the budget deficit for recurrent costs for the rest of 1999 and 2000. To re-staff primary health care, UNMIK/WHO will need to develop a plan to re-deploy staff who have migrated to the hospital sector. Doctors in primary health care clinics and other primary health care staff with higher qualifications should receive some incentive payment, higher for those working in rural areas. Trainee specialists should be paid less than primary health care doctors.

25. **Investment in Works and Equipment.** Reconstruction and equipment of damaged primary health care facilities is a high priority for physical investment. Some grouping together of the many small primary health care clinics should occur during reconstruction. While

upgrading and re-equipping of six district hospitals is also needed, there should be no further investment in new or enlarged hospitals. Some downsizing is needed over the medium-term.

26. **Training.** Retraining and accreditation (in co-operation with the Prishtine Medical School) is needed for parallel system graduates who received little opportunity for training in clinical skills. Initial training should orient these doctors and nurses towards primary health care, as a precursor to more comprehensive training in family medicine and nursing practice. Also, skills enhancement and continuing medical education needs to be offered to specialists and other health professionals who have not been required or able to receive this type of training in the past 10 years. Management training throughout the sector should begin, using short courses initially, pending development of formal diploma and degree programs in management.

27. **Technical Assistance.** Technical assistance is needed to re-build the functions of policy and planning (the future Ministry of Health), public health (the Institutes of Public Health), and health insurance (the Health Insurance Fund). Donors have been identified to support the first two areas, but redevelopment of the Health Insurance Fund remains a critical unmet need. Plans need to be developed to restore the revenue-raising functions of the Health Insurance Fund as soon as possible. This will require training Health Insurance Fund staff to carry out budgeting, resource allocation, monitoring and control functions, as well as preparation for medium-term development of better provider payment arrangements. Also, technical assistance should identify fairer and more transparent official policies on user co-payments, both to raise revenue and to discourage existing informal out-of-pocket payments.

Medium-Term Development Policy

28. Four areas of policy development are crucial in the environment described above:

- shifting health spending for clinical services from tertiary care facilities to district and local health infrastructure for primary health care and essential secondary care;
- reducing waste and inefficiency in public sector health service delivery and other health programs;
- investing more resources in highly cost-effective public health activities that can substantially improve the health of the population, in particular that of the poor;
- increasing community control and financing of essential health care, and building the local institutions required to carry out these functions.

Better Allocation of Spending on Clinical Services

29. District health infrastructure needs to be developed to increase the share of patient care managed in primary health care, to assure access to functioning essential hospital services, and to build the capacity to plan and manage health services at the district level and in individual facilities.

30. There are several elements to this development:

- upgrading a rationalized network of health centers and dispensaries to provide modern primary health care/family medicine;

- developing training programs for primary health care providers, particularly nurses and midwives;
- refurbishing and equipping essential services in down-sized district hospitals;
- establishing an ambulance system to cover the whole of Kosovo;
- building capacity to plan and manage health facilities at the district level and in individual facilities;
- creating financial incentives to motivate this shift of resources.

31. The WHO strategy recommends that primary health care clinics should be consolidated into group practices of around five doctors, ten nurses plus ancillary staff, serving a population of around 10,000. It is anticipated that some care will continue to be provided by private practices. WHO recommends that health houses gradually be transformed into larger primary health care clinics (rather than an additional level of care), with additional diagnostic facilities and perhaps visiting specialist clinics.

32. As the WHO strategy proposes, no expansion of existing hospital capacity is required, and modest efficiency gains would allow some downsizing while sustaining current caseload. New investment in central hospitals should be limited toward reorienting those activities to an appropriate tertiary caseload (with less complex cases treated at district level or primary health care), treated more efficiently, and to clinical teaching and research.

33. Resource allocation tools and provider payment mechanisms need to be developed which support the strategy of treating more patients in primary health care, and at the district rather than central level. Financial incentives in the salary structure for doctors and nurses also need to be put in place to encourage health workers to take up primary health care (particularly in rural locations), and to make secondary and tertiary specialization relatively less attractive.

34. In the short- term, WHO and a range of donor agencies and NGOs propose to offer short-course training to provide orientation and basic training for doctors in primary health care/family medicine. The aim is to encourage a large share of the parallel system graduates and other returning medical school graduates to shift into primary health care. This type of training will need to be supplemented by a more medium-term approach, in order to provide a good quality primary health care system, and to raise the status of family medicine in a credible way. It is essential to make an early start in establishing a qualifications framework and curriculum for family medicine specialization, in conjunction with the Medical School in Prishtine University. Although a proper family medicine program will not yield graduates for three years or more, an early commitment to establish a credible qualification of this sort will add to the incentives for capable medical graduates to choose primary health care as a career path, and will also enable donors and NGOs to link their training activities to a comprehensive curriculum.

35. To meet essential health needs, a greater share of the health budget needs to be devoted to the operation of lower level facilities. Initial emphasis needs to be placed on building capacity in primary health care to deliver services which address the most common health problems, including Kosovo's specific post-conflict needs and problems arising from past lack of access to public services. There may be value in defining a basic set of services to be managed in primary health care. Both communicable diseases (tuberculosis and vaccine-preventable diseases) and non-communicable diseases have to be addressed in primary health care. As a consequence of

the conflict, there is high need for conflict victims rehabilitation through a community-based approach. In addition to the need for mental health interventions for conflict victims, primary health care needs to be equipped to manage serious mental illness, given the lack of psychiatric services in Kosovo, and the return of a number of Kosovar patients from long-term psychiatric facilities in Serbia.

Reduction of Waste and Inefficiency

36. Two areas stand out in which there is substantial scope for reduction of waste and inefficiency:

- In Central European countries, pharmaceuticals typically account for 15-30 percent of public health spending, and a large share of private out-of-pocket spending. Significant savings and improvement in the safety and efficacy of treatment can be achieved through use of an essential national drug list, and through purchasing drugs competitively. WHO and PSF have collaborated in producing an essential drug list for primary health care, and work is underway on development of an essential list or formulary for hospitals.
- Kosovo has too many hospital beds for the number of hospital admissions used, and with a modest reduction in length of stay from 12.5 percent, and some increase in occupancy from 75 percent, could support a reduction in the bed size of Prishtine hospital and the five district general hospitals. Larger hospitals tend to duplicate facilities, such as pharmacies, laboratories and diagnostic imaging, and functions such as procurement and inventory management, which should be centralized to improve efficiency. The WHO proposals for consolidating the small dispensaries into larger primary health care practices should increase quality (e.g. enabling primary health care to provide 24 hour coverage), and make more efficient use of a wider range of equipment. Kosovo needs to ensure that many of the doctors who have recently moved into hospitals are redistributed to primary health care, with good geographic coverage. This will mean a reduction in the number of trainee specialists. The clinical and managerial skills of health personnel need to be substantially upgraded and reoriented from the previous system of centralized bureaucratic control towards an emerging system or more autonomous health facilities.

37. The current legal and regulatory environment for private medical practice and pharmacy and payments of fees to doctors appears to be weak or non-existent. Medical malpractice, unsafe or poor quality pharmacy practice and financial fraud are a significant risk with growth in the number of private medical practices, private pharmacies and semi-private practice in public hospitals (for patients who pay informal fees). Since government regulatory capacity is likely to be weak in the next few years, health system reforms should be designed in ways that minimize the need for direct government regulation. Encouraging self-regulation through professional associations of doctors, pharmacists and hospital managers would be one such approach. Urgent mechanisms for enforcing safety-related sector legislation need to be established by UNMIK using local resources where feasible, such as the Institute of Public Health. In the medium term, better regulation will require both training of government inspectors and other regulatory personnel and development of government institutions, such as professional licensing boards and ethics committees.

Investment in Public Health and Priority Health Programs

38. In view of Kosovo's young and fast-growing population, reproductive health services and child health services are of high priority. These programs include safe motherhood, family

planning and well childcare, and should combine education with primary health care/community-based intervention. Increasing rates of immunization completion is a very high priority. UNMIK/WHO have already re-started the immunization program. Among communicable diseases, tuberculosis and gastrointestinal infections remain at high rates in Kosovo. Among non-communicable diseases, there appears to be high prevalence of diabetes and renal disease. Other public health activities with a large payoff for health status are anti-tobacco measures (excise tax, advertising restrictions, anti-smoking campaigns), food safety measures, and some environmental health measures (drinking water safety, sanitation).

Community Control and Financing

39. In the past, health expenditures were financed principally from pay-roll tax contributions to the Health Insurance Fund. There were also limited patient charges which covered part of the cost of some services (for prescription drugs, orthopedic appliances, eyeglasses), with exemptions for some classes of patients (children, students, people over 65). Patients have paid an increasing share of the costs of care by direct out-of-pocket payments to practitioners, either through informal “under-the-table” payments to doctors, or through use of private practitioners and private pharmacy. Public expenditure on health amounted to 3-4 percent of GDP in 1989. This share of expenditure today, with a much lower GDP and the loss of revenue redistributed from richer to poorer regions within FRY, would see Kosovo spending of the order of \$18-26 per capita a year-- enough to purchase a minimum package of care costed for low-income countries. Kosovo currently enjoys a higher level of care. The health budget proposed by WHO to maintain the existing system (see below) amounts to around US\$42 per capita (in the range of 5.5-8.4 percent of GDP). Kosovo will therefore need to spend a higher share of GDP on health than in the past, through higher contribution rates or higher patient charges, if it is to finance a package of public health measures and essential clinical services of the sort proposed by WHO.

40. The examples of other countries in the region could help Kosovo health authorities to re-establish a health insurance system that preserves the main virtue of the pre-1990 system – widespread population coverage – while improving transparency and creating incentives for efficiency. Almost all Central European countries finance health care through compulsory payroll tax contributions to Health Insurance Funds, often supplemented with some revenue from the general Government budget. Other country experiences provide some lessons on how best to combine revenue from different sources (compulsory insurance contributions, budget revenues, voluntary insurance, patient charges) to produce a stable and sustainable financial base for the health system, with incentives for financial control and efficient service delivery.

41. It is likely that Kosovo will want to restore a system of compulsory health insurance contributions. It is also likely to be necessary to make some use of patient charges, preferably at a modest level, with targeted exemptions and safety nets to assure access. It is highly desirable in the medium-term to end the illegal practice of doctors asking for “under-the-table” payments from patients, and to discourage doctors in the public sector from diverting patients to their private practices. It must be acknowledged, however, that this objective is unlikely to be achieved quickly or easily. In view of the limitations on capacity for Kosovo to raise general taxes, high priority should be given to planning for restoring the Health Insurance Fund’s revenue-raising functions and to re-instituting co-payment arrangements.

42. Policies to govern the distribution of health revenue to different districts and health care providers across Kosovo, and the mechanisms for paying health care providers will need attention in the medium-term. In the first six to eighteen months it is likely that providers will be reimbursed for the costs of inputs (salaries, pharmaceuticals, other supplies, capital), based on

approved plans for staff numbers, approved capital investment and so on. In the medium term, mechanisms should be developed for paying providers for defined outputs (such as numbers of patients registered with a primary health care clinic, numbers of hospital admissions for different conditions), subject to a global limit on their budgets. Ideally, providers should also be given some incentives to improve the quality, efficiency and effectiveness of their services. The former system for paying providers tended to encourage inefficiency (for example, by encouraging long lengths of stay in the hospital, and excessive numbers of doctor consultations) and should not be re-instituted.

43. To develop local capacity for health sector revenue collection, distribution and provider payment as early as possible, the Health Insurance Fund is high priority for institutional development. There is undoubtedly a large training and development task required, but in the interim, there will be benefits from engaging the Health Insurance Fund in the process of budgeting, revenue distribution and provider payment, and in the task of planning for restoration of its full functions. It may make sense to allocate some or most of UNMIK's general budget funds for health through the Health Insurance Fund, beginning sometime in FY2000.

44. In developing local institutions for management and oversight of the Health Insurance Fund and health service delivery system in Kosovo, the question of the appropriate degree of fiscal and administrative decentralization needs specific consideration. Decentralization of public health services is often seen to be potentially the most important force for improving efficiency and responding to local health needs and conditions in former socialist economies. It can be successful, however, only when local government health agencies and providers have sound financial bases, solid administrative capacity, incentives for improving efficiency, and accountability to patients and local citizens. Hasty decentralization, or decentralization to too small a unit of government, can create inefficiencies.

45. The average municipal population is too small to make efficient use of general hospital services, or to pool financial risks (the risk that some of the population will require very high cost health care), or to distribute revenue fairly across high and low-income populations. The average population in each of the five districts in Kosovo is too small to support efficient tertiary services, which can only be provided at the province-wide level (or for some highly specialist services, by referral to larger hospitals outside Kosovo). The Health Insurance Fund functions of pooling financial risk and redistributing revenue from higher to lower income areas should be centralized at the province-wide level.

46. The health sector is likely to be better served by a single Health Insurance Fund with five or six district branch offices (and some municipal branches if manual systems of tax collection and payment of cash benefits continue), than by a more decentralized approach to financing. Policy, planning and regulation functions for the health sector are best carried out at the province-wide level. There is room for debate about whether there are benefits from more decentralized ownership of health care facilities, but problems tend to arise if hospitals are owned by municipalities of the relatively small average size in Kosovo. Municipal ownership of primary health care facilities creates fewer problems, though the benefits of local ownership (such as greater community support) need to be weighed against the benefits of common management for both primary health care and secondary health care (better co-ordination, stronger clinical and managerial support).

Implementation

47. WHO is already leading donor co-ordination, and has already issued interim policy guidelines which should be used by donors and NGOs as a basis for setting priorities and adopting a coherent approach to rebuilding the sector in Kosovo. A lead NGO in each sector is playing a coordinating role for humanitarian effort in the health sector. These initial coordination arrangements should be strengthened as the reconstruction program gets underway. While individual donors will want to operate their own project implementation arrangements, stronger coordination is vital to mitigate risks that emerged in the post-conflict environment in Bosnia and Herzegovina, and which are already emerging in Kosovo, of inappropriate and unsustainable investment. WHO should be mandated to establish an Aid Coordination Unit for the health sector, under the auspices of UNMIK, with the authority to coordinate implementation and ensure that policy guidelines are followed, in the interests of rational priorities and sustainable sector development. Donors should be encouraged to co-finance larger programs, use established NGOs as implementation agencies, or establish other joint implementation arrangements where possible, to reduce the burden of project management costs.

C. COST ESTIMATES

Recurrent Budget Requirements

48. UNMIK is progressively paying stipends to health sector workers, which are intended to be humanitarian assistance, not a salary or recognition of employment rights. Donor commitments have been received which cover the August stipend payments and two-thirds of the drugs bill (some US\$3.9 – 4.4 million) for the rest of 1999. However, because much donor assistance is tied to particular locations and purposes, there are some urgent needs for revenue in other locations. Further un-hypothecated donor assistance is needed to permit rational expenditure priorities to be met.

**Table 2. Stipends in the Health Sector
(in US dollars)**

	August stipends
Doctors, specialist and non-specialist	195
Nurses, technicians	83
Support staff	56
<i>Average net pay</i>	<i>99</i>

49. For the year 2000, UNMIK is preparing a budget for the recurrent annual costs of maintaining the Kosovar health system, drawing on the work of WHO, but scaling back some areas of expenditure in view of likely affordability constraints. This budget should be available in the coming weeks. Based on experience in other countries, attention should be paid to ensure that both salary and non-salary expenditures are funded at adequate level. In particular, a provision should be made to ensure the financing of pharmaceuticals and other non-salary recurring expenditures (e.g., heating) at a level that makes it possible to deliver proper health care services.

50. In the next phase of more detailed budget planning, it is vital that explicit provision is made for the Public Health Institutes, Health Insurance Fund, and future Ministry of Health

functions. Donors have tended to overlook these critical elements of local capacity, which must be rebuilt to enable hand-over of responsibility to the Kosovars for health sector administration as early as possible. In budget execution and payments functions, it is vital to give priority to primary health care and to these management functions, rather than paying hospitals first.

51. **Revenue Collection Issues.** If the health sector is able to raise some revenue internally (for example, through modest patient charges (“co-payments”) for prescription drugs and orthopedic appliances), a higher level of expenditure could be supported. It should be possible to raise US\$5-6.7 million annually from a simple co-payment regime. Co-payments could finance some 20 percent of prescription expenditure, even with exemptions or nominal charges for a significant share of needy patients, thereby raising US\$3.3-3.9 million annually. Similarly, a modest daily charge to cover “food and lodging” costs for hospital inpatients, could raise on the order of US\$1.7 –2.8 million annually. WHO plans to develop recommendations on health financing policy in the next three months, including consideration of whether co-payments will be needed.

52. In the medium-term, the major share of health sector revenue, however, will need to come from contributions from general budget revenues and/or health insurance contributions. It is a very high priority to restore the system of health insurance contributions, the bulk of which can be expected to come from payroll tax. Putting in place effective mechanisms to collect contributions from farmers, the self-employed and small businesses will be more difficult. Nonetheless, early planning and technical assistance is needed on how to set up more effective systems for collecting health and other social insurance and tax contributions from these sectors.

53. There may be benefits from hypothecating a portion of general budget revenues (derived from donor sources and customs and excise taxes) for the Health Insurance Fund as soon as basic Health Insurance Fund functions can be restored, during the course of FY 2000. This would enable the Health Insurance Fund to develop its provider payment functions at an early stage, alongside planning for restoration of its revenue collection functions. If some local revenues (municipal) become available for health expenditure, general budget revenues from the central budget should be used to improve equity and pool risks across municipalities.

Capital and Other Investment Expenditure for a 3 - 4 Year Reconstruction Program

54. Detailed surveys of capital requirements and training needs will be completed by December 1999. A preliminary estimate of the costs of a three-to-five year program of upgrading capital and personnel skills, and strengthening local institutions is summarized in the table below. Although cost estimates are only indicative, the priorities listed in the program provide a clear starting point for donor-financed activities, and are consistent with the WHO strategy. The cost of repair to conflict-damaged clinics is derived from a preliminary (July) EC/IMG survey, and needs to be updated. WHO proposes that primary health care clinics should be consolidated into a smaller number of larger centers, each with around 5 doctors, 10 nurses and ancillary staff. This would entail upgrading around 180 clinics, but at a higher cost per clinic than assumed by EC/IMG estimates.

55. The table does not attempt a detailed costing of a number of desirable development programs. A number of developments related to specific sub-sectors (including: nursing education, community-based rehabilitation, mental health services, reproductive health services, pharmaceuticals regulation and procurement, tuberculosis control) have been identified as priorities in WHO’s proposed strategy for the health system for Kosovo. Action plans in these

areas are being developed by WHO, and costing of programs will take place over the next two to three months. Costings below are indicative aggregate estimates only.

**Table 2: External Financing Requirements for the Health Sector
(in millions of US dollars)**

Activity	First Phase (until December 2000)			Second Phase (2001-2003)	Total
	Until March 2000	April to Dec. 2000	Total		
INVESTMENTS					
<i>Civil Works</i>					
Damaged PHC Clinics	3.0	4.0	7.0	1.0	8.0
Hospitals and other PHC Clinics	0.0	5.0	5.0	13.0	18.0
Other (HIF, Training Sites)	1.5	0.5	2.0	0.0	2.0
<i>Equipment</i>					
Damaged PHC clinics	1.0	1.0	2.0	2.0	4.0
Hospital Equipment	6.0	8.0	14.0	13.0	27.0
Ambulance System	1.0	1.0	2.0	3.0	5.0
<i>Priority Health Programs</i>	1.0	2.0	3.0	6.5	9.5
Subtotal	13.5	21.5	35.0	38.5	73.5
TECHNICAL ASSISTANCE	2.5	2.5	5.0	6.5	11.5
Total¹	16.0	24.0	40.0	45.0	85.0

¹ In addition, about US\$43 million will have to be funded through the budget for operating expenditures in the sector.

ANNEX VIII: TELECOMMUNICATIONS

A. SECTOR DESCRIPTION

1. With only about 130,000 phone lines in service, Kosovo's telecommunication network has the second lowest telephone penetration rate in Europe, amounting to about 6 lines per 100 persons (about a quarter of the FRY average of 22 per hundred people).¹ Since very little investment was made in the sector through the 1990s, the current network is little different from that of 1989. Only 34 percent of the network is digital, and the remainder is obsolete crossbar (53 percent), or step-by-step (13 percent). About 20 percent of analogue customers are on party lines where two customers share the same connection from the exchange. Almost all exchanges are interconnected via a tandem exchange in Prishtine, over a largely star-configured analogue microwave transmission network. The interconnection between Kosovo and the rest of FRY is ensured via the Prishtine tandem exchange through an optical fiber cable and an analogue microwave route. This same routing is also used for all international traffic via the international exchange in Belgrade (although there is also a cross-border connection to the Former Yugoslav Republic of Macedonia). The telephone numbering plan in Kosovo is integrated with the whole of the Republic of Serbia.

2. Prior to 1989, the entity operating Kosovo's telecommunication network was combined with the postal service. After 1989, there were a series of changes in the institutional structure: (i) in 1989, the Kosovo telecommunication entity was subsumed within the Posts and Telecommunication Department of the FRY Ministry of Communications; (ii) subsequently the Republic of Serbia telecommunications was separated from posts and then established as a joint stock company, Telecom Serbia; (iii) in 1997, forty-nine percent of Telecom Serbia was sold to a consortium of Telecom Italia and OTE (the national telecommunications operator in Greece). In parallel, Telecom Serbia was awarded a GSM license. Currently, the only mobile service in Kosovo is from a private operator, Mobtel which has both an analogue and a GSM license via a remote antenna on the "new" telecommunication center in Prishtine, connected to the mobile switching center in Belgrade by optical fiber cable. Mobtel has roaming agreements with all major GSM operators throughout Europe.

B. CURRENT SITUATION

Conflict-related Damage

3. Telecommunications infrastructure suffered heavy damage to key installations during the conflict. Communications on the fixed network is limited to local calls. International access is not available except for very limited service on a few exchanges in Pristine. Despite the two mobile licenses issued by FRY for the Republic of Serbia, there is no mobile service in Kosovo except in Prishtine.

4. Many facilities were fully destroyed, including:

- A local exchange, Prishtine 2, with a capacity of 10,000 lines (all other local exchanges are in service) – resulting in difficulties for communications within Prishtine;

¹ Teledensity in the region is typically at or around 30 percent, and in Western Europe over 40 percent.

- The tandem exchange in Prishtine and the two nodal transmission stations (Golesh and Cviljen) providing interconnection between the local exchanges – and hence there is no inter-city telephone service throughout Kosovo; and
- Two other secondary transmission stations at Grimija and Bojero.

The only remaining connection to the FRY network, including access to the international exchange, is via 3x2Mbit/s blocks (90 circuits) carried over a very vulnerable optical fiber cable, which is exposed in places on the roadside and has already been broken once.

5. Whilst the local exchanges remain in service, in most cases, there are no spare parts and there is no test equipment, tools or vehicles for rehabilitation and maintenance. Only those exchanges at nodal points (e.g. Prishtine, Mitrovica, Peje, Prizren, Ferizaj, Gjilan and Gjakova) have standby power plants. All other exchanges are likely to fail if power outages exceed their battery capacity. There are no firm estimates of the number of subscribers lines/installations that were destroyed during the conflict, but it is thought that some 110,000 lines remain in service.

Institutional Situation

6. Immediately after cessation of the conflict, pre-1989 Kosovar Albanian management staff reclaimed their former jobs, and proposed to restore a combined Post and Telecommunications entity, “PTK” (Posts and Telecommunications of Kosovo). The network is operated under UNMIK supervision by about 350 local staff (half of the pre-1989 workforce). Workers are currently not receiving salaries – and telephone service has not been billed since June. UNMIK recently announced an agreement concerning future billing arrangements for telephone service.

7. On the basis of UN Resolution 1244, the International Telecommunications Union (ITU) has denied Kosovo a separate country code, as well as representation within the international telecommunications fora. Kosovo cannot enter into a operating relationships with foreign telecommunication operators (unless it is permitted to do so by the appropriate FRY authorities). Through its regulation 1999/12, however, UNMIK has established PTK as a “juridical entity” and given it the right to use all present and future telecommunications assets in Kosovo (although it does not confer ownership rights). The regulation also established a Joint Civil Commission on Postal and Telecommunications Services to supervise and provide policy guidance to PTK.

8. Macedonia Telecom, Slovenia Telecom and British Telecom have provided assistance/training to PTK. In addition, British Telecom has provided a supplementary international telephone service. However, because it was unlicensed, BT was not able to charge for the service, which has been suspended until the licensing issue is resolved.

9. Various suggestions have been made for providing an expedient mobile GSM telephone service to alleviate the present lack of inter-city telephone service by, in effect, making coverage in Kosovo part of another country’s mobile service and using that country’s international prefix. This would be technically simple, but UNMIK would have to resolve legal requirements regarding frequency allocation and operating licenses.

Regulatory Issues

10. A number of regulatory issues need to be addressed for successful recovery in the sector. UNMIK will play a key role, and donors may consider providing expertise in critical areas, as needed. Key issues include: (i) obtaining necessary authorizations to establish international

relationships/access to foreign operators; (ii) giving the necessary authorizations to develop a mobile GSM service throughout Kosovo (also taking into account already-issued licenses); (iii) re-establishing billing for telephone service; (iv) reaching an agreement for payment of calls to the rest of FRY (and international calls); and (v) creating an entity that can receive donor funding while ownership issues are being resolved.

Sectoral Priorities for Recovery

11. A rapid rehabilitation of the telecommunications network is key for successful recovery, since the current situation may hamper the restart of large-scale economic activity. In principle, telecommunications is an income-generating activity, and some part of the development program could be financed from private sources. It is expected that the private sector could and should play a leading role in the development of a functioning GSM service, and in part of the modernization effort. Still, in view of the urgency of the situation, the extent of damage and the poor development of the network, as well as the current uncertainties concerning Kosovo's political status, some donor support will be needed for repair of the fixed network and to catalyze private sector activities. Such support should be heavily frontloaded, so as to allow for a rapid resumption of telecommunications in the region.

12. Priorities for external support include:

- Repair of the damage to the existing network, including: (i) restitution of the long distance microwave network (SDH 6-7GHz); (ii) replacement of the Kosovo tandem switch (2,000 trunks); (iii) rehabilitation of the Prishtine local exchange; and (iv) repair of the local distribution network (including civil works).
- Provision of spares (possibly available from suppliers), tools, test equipment and maintenance vehicles;
- Limited modernization of the network, to replace obsolete analogue exchanges with digital ones, and to double the network capacity to 250,000 lines, increasing teledensity to 12 percent;
- Establishment of independent international access (including a 2000-trunk international exchange) for Kosovo in addition to access already provided via FRY (there are several technical options, notably via the Trans-Balkans Line which links Bulgaria and Albania, and provides access to undersea optical fiber cables to the rest of the world);
- Adequate mobile coverage throughout the region (for a total capacity of about 30,000 consumers), to meet demand that cannot be satisfied by the fixed network;
- Restoration of billing for telecommunication service, which requires, among other things, the provision of computer equipment; it is expected that user charges will cover all operating expenditures as soon as payment is re-established and inter-city and international service is restored; and
- Technical support to the telecommunications operating entity, whose staff has little experience of modern technology, management, markets and market norms.

12. In view of the urgency of the needs, adequate implementation mechanisms should be designed that would allow early resumption of adequate service, while respecting the interests of

the various entities legitimately involved in the sector. An option would be for UNMIK to establish a legal entity to receive donor funds and invest in equipment; this entity would then lease or otherwise make available this equipment to the operator of the fixed network.

**Table 1: External Financing Requirements for the Telecommunications Sector
(in millions of US dollars)**

Activity	First Phase (until December 2000)			Second Phase (2001-2003)	Total
	Until March 2000	April to Dec. 2000	Total		
INVESTMENTS					
Microwave Repair	6.0	0.0	6.0	0.0	6.0
Replacement Tandem Switch	2.0	0.0	2.0	0.0	2.0
Local Network Repair	2.0	3.0	5.0	0.0	5.0
Spares/Tools/Test Equipment	2.0	2.0	4.0	0.0	4.0
Vehicles	2.0	3.0	5.0	0.0	5.0
Independent International Exchange	0.0	2.0	2.0	0.0	2.0
GSM Mobile Network	0.0	15.0	15.0	0.0	15.0
Network Modernization and Expansion	0.0	0.0	0.0	55.0	55.0
Subtotal	14.0	25.0	39.0	55.0	94.0
TECHNICAL ASSISTANCE	0.5	1.0	1.5	0.5	2.0
Total	14.5	26.0	40.5	55.5	96.0

ANNEX IX: ENERGY

A. SECTOR DESCRIPTION

Pre-conflict Situation

General

1. Electricity, primarily from lignite-powered thermal power plants, has been Kosovo's main source of energy. Other sources of energy have been district heating systems in four cities, and coal for use by industries and households. Coal for the thermal power plants and for other uses came from one of Europe's largest surface lignite deposits near Prishtine. Electricity is widely used for all household purposes, including space heating where district heating is not available. In the pre-conflict period, about 30 percent of the electricity was used by industrial consumers, mainly by the two large metal-mining entities, Feroniki and Trepca. Kosovo used to be an important net energy exporter, feeding into the high voltage transmission ring of the former Socialist Federal Republic of Yugoslavia (SFRY).

Power

2. The total installed generation capacity was 1,495 MW, provided by two large lignite-fired thermal power plants near Prishtine (Kosovo A and Kosovo B) and one hydropower plant at Gazivode. The Kosovo A thermal power plant has five units with a total installed capacity of 800 MW (1x65 MW, 1x125 MW, 2x200 MW and 1x210 MW); whereas the Kosovo B thermal power plant has two units with an installed capacity of 660 MW (2x330 MW). Even in the pre-conflict period, the thermal power plants were in poor condition and the actual available capacity was significantly less. The Gazivode hydropower plant has two units of 17.5 MW each and was in reasonably good condition.

3. Reliable data on electricity generated, generation costs and consumption patterns is not available. Kosovo is stated to have produced 4,912 GWh of electricity, of which 2,907 GWh was for domestic consumption and the remainder for export outside the province. The maximum peak demand was 546 MW in January and the minimum was 362 MW in July. For 1997, electricity production is stated to have been 4,318 GWh, of which 3,502 GWh was for domestic consumption. Total losses are stated to have been about 30 percent.

4. Before the conflict, the Kosovo power system, being part of the FRY network, was controlled by the Union of Yugoslav Electric Power Industry's (JUGEL) dispatching center in Belgrade, except for distribution networks which were controlled locally. Power exchanges with neighboring countries were also controlled by JUGEL.

5. Distribution networks were controlled by decentralized distribution companies and divided into seven areas: Ferizaji, Gjakova, Gjilani, Mitrovica, Peja, Prishtine and Prizreni. The total number of consumers was about 360,000. The total length of transmission lines (110 kV and higher) was 1,085 km, and of the distribution lines (35 kV and lower) was about 29,000 km. Transmission and distribution transformer capacity was about 4,600 MVA. The backbone of the interconnected transmission system is a 400 kV network, which is interconnected with FRY and, the Former Yugoslav Republic of Macedonia. There is also a 220 kV interconnection with the Former Yugoslav Republic of Macedonia, Serbia and Albania.

Coal

6. Coal is extracted from two large mines, Mirage and Bardh. They are large surface mines, extracting lignite under favorable overburden/coal ratios with the 'continuous' mining method, which uses bucket wheel excavators and conveyors for the extraction and transport of overburden and lignite. The mines are at an advanced stage of development and all overburden is now dumped inside the pits. The mining fronts of the two mines are approaching each other, and in about 6 years, the two pits will be joined as a single mine with a West and an East wing.

7. The design capacity of the two mines was estimated at 16 million tons per year. In 1989, the two mines produced 10.5 million tons of lignite. In the preceding five years (1983-1988), the Kosovo mines had enjoyed the highest growth rate of all former SFRY coal mines, a production increase of 41 percent, compared to an average increase of 20 percent for the whole territory of the former SFRY during that period. Kosovo's share in the coal supply of the SFRY was 18 percent in 1989. About 85 percent of the Kosovo lignite produced was consumed for power generation in the Kosovo A and B Power Plants, and the remaining 15 percent was for industrial and household use.

8. From 1989 onward, the production of the Kosovo mines dropped gradually to about 8 million tons per year. A further drop, to about 6 million tons per year occurred in 1993 and 1994, during the Bosnian conflict. Thereafter, in the second half of the 1990s, production recovered to a level of about 7 million tons per year. The variations in production are probably the result of the combined impact of reduced power demand in Serbia, production difficulties at the Kosovo power plants and mines, and possibly also the deliberate shifting of coal production to FRY.

9. Employment at the mines was kept at about 2,500 in both mines, a high figure compared to international standards, resulting in poor labor productivity for a mining method which is designed for high output and labor productivity. In 1989, a separation of the workforce into Kosovar Albanians and Serb Kosovars was introduced by moving Albanian Kosovar workers to the Bardh mine and Serb workers to the Mirage mine. Production from the Bardh mine was reduced drastically (the output of the Bardh mine dropped from 6.1 million tons in 1989 to 3.1 million tons in 1990), while the output from the Mirage mine was increased. Apparently, some replacement investments have been made (in particular in the older Mirage mine) and the main equipment has been kept in operable condition.

10. The costs of Kosovo coal production in 1987/88 were reported to be US\$ 8.5/t, compared to an overall average coal production cost of US\$ 17.0/t for SFRY at that time. The costs of Kosovo lignite production included about 25 percent personnel costs, 25 percent costs of supplies (spare parts, materials and energy), 25 percent depreciation and 25 percent other costs. It is likely that true costs, calculated in accordance with international standards, were higher, considering the poor standards in financial and environmental management, the inflationary environment and a political motivation to show high performance and low cost figures.

11. No data on financial and technical performance are available for the years after 1989. Most of the usable mobile equipment was also removed from the mines and workshops.

12. The quality of the Kosovo lignite is poor. The average heating value is 6,700 kJ/kg (or 6.7 GJ/t). The average ash content is about 25 percent and the average moisture content 50 percent. However, the sulfur content is below 1 percent. Despite its low heating value, Kosovo lignite is believed to be an economic fuel. At the reported 1988 production costs, the heat-based cost of Kosovo lignite is US\$ 1.3/GJ. Even under the assumption that the true costs are 50

percent higher than reported in 1988, the costs at US\$ 1.9/t, would still be favorable compared to an estimated US\$ 2.0/t for internationally-traded coal landed in Western Europe.

13. The low costs are the result of a favorable overburden to coal ratio (less than two parts of overburden for one part of coal) and a massive deposit with one single coal seam of about 50 m thickness, containing several billion tons of coal reserves. These conditions allow the application of large-scale, low-cost surface mining methods. Production in the Mirage surface mine started in the early 1960s and was scheduled to supply the Kosovo A Power Plant. The Bardh mine started coal production in the early 1970s and was scheduled to supply the Kosovo B Power Plant. In the mid-70s, the SFRY Government had already elaborated plans for the development of a lignite-based power generating capacity of about 10,000 MW in Kosovo. It was seriously considering the first expansion of generating capacity beyond the Kosovo A and B power plants in the early eighties, but decided in the late eighties to expand instead power generation capacity at Kolubara, in Serbia's largest coal basin south of Belgrade, which has less favorable geological conditions for mining but a better track record in mining performance.

District Heating

14. Pre-conflict, Kosovo had district heating (DH) systems in Prishtine (162,000 inhabitants), Gjakova (78,000 inhabitants), Mitrovica (64,000 inhabitants) and Lipljan (68,000 inhabitants). All systems were run by municipal-owned district heating enterprises (DHEs), which ensured the supply and distribution of heat. DH is produced in heat-only boiler plants and fired mainly by imported heavy fuel oil (mazut), and by domestic coal. The district heating facilities supply the most densely inhabited part of the cities and public facilities such as hospitals, schools and administrative buildings. Mazut for the boilers used to be provided through Serbia. The DHE of Prishtine had a primary distribution length of about 28 km and provided heat to about 80,000 consumers. The output of the boilers is 116 MWt (2x58), with another 29 MWt boiler non-operational. The output of the Gjakove boilers is 36 MWt, and that of Mitrovica is 11 MWt. All DH systems delivered heat only and did not provide domestic hot water. As a result, all networks were only operated during the heating season, which usually covers the period of October 15 to April 15 depending on local conditions.

15. DH prices were well below production costs. While consumption by public facilities such as hospitals, hotels and administrative buildings were metered, households were invoiced based on an average charge per square meter of living space. Two tariff rates were used: 2 DEM/m² for commercial and industrial consumers, and 1 DEM/m² for residential consumers. The production cost for heat is estimated to have been about 3 DEM/m², with the municipalities subsidizing the difference.

Current Situation – Physical Status

Power

16. **Generation.** The power plants have suffered mainly from lack of maintenance and mismanagement, but there has been no direct conflict-related damage. The Kosovo A thermal plant is designed to cover domestic demand through the 220 kV and 110 kV transmission network. The plant is nearing the end of its useful life and has been subjected to prolonged negligent operational practices and lack of maintenance. The environmental standards at the plant are hazardously low, and there are abundant signs of poor housekeeping practices and safety standards. Out of five units, only one or two operate intermittently and at reduced capacity. Cannibalization is often resorted to because of lack of spare parts. A significant amount of costly

diesel fuel needs to be added to the coal to maintain combustion in the units. Each re-start of one unit consumes an extra 75 tons of diesel, which increases the cost of operation. The Kosovo B thermal plant was designed mainly for power export at 220 kV and 400 kV. The power plant is about 15 years old (mid-life), with a production expectancy of another 15 to 20 years. The plant is at present not in operation due to problems in water treatment, turbines, a missing boiler circulating pump, and due to the high activation energy required to re-start the units. With a relatively minor overhaul and repair program, both units could be re-started. However, the plant does not have black start capability, and the start-up power would have to be supplied via the 220 kV transmission system, either from Albania, the Former Yugoslav Republic of Macedonia or from Kosovo A. The Gazivode hydropower plant is in reasonably good condition and can operate at full capacity.

17. **Transmission.** The high voltage 400 kV transmission network that connects Kosovo to Montenegro and Bosnia and Herzegovina in the West, to Serbia in the North, and to the Former Yugoslav Republic of Macedonia and Greece in the South, is out of operation. The 220 kV network is in poor condition. The restoration of the 220 kV lines, in particular to the Former Yugoslav Republic of Macedonia and Albania, is very important for stabilizing the transmission grid and for allowing power exchanges, and has become critical in the absence of a functioning 400 kV grid. Power exchange with Serbia via the 220 kV network is desirable, but cannot be counted on under the existing political circumstances and with much of the Serbia power grid being out of operation. The 110 kV ring network is vitally important for serving the country's domestic demand, but significant parts are out of service. In the South and South-West of Kosovo, entire areas are cut off. The 110 kV network also carries limited power exchange with Serbia. There are serious stability concerns about the transmission network of the entire region, and there have been several incidents of system collapse in one country triggering system failures in neighboring countries.

18. **Distribution.** Conflict-related damage to the secondary distribution network is extensive, estimated to affect 30 percent of the network. Damage is particularly extensive in the Gjakove, Gjilan, Mitrovica, Peja and Prizren areas. Rehabilitation of a major portion of the damaged network is urgently required before the coming winter. In certain areas, de-mining operations will have to be carried out before rehabilitation can be undertaken. The distribution companies suffer from lack of tools, vehicles and equipment, all of which are essential for maintenance purposes.

Coal

19. There is no conflict-related physical damage to the mines. However, basically all mobile equipment has been removed from the sites. Principally, the main mining equipment is in operable condition. This has been confirmed by testing of the equipment. Maintenance of the main equipment apparently has been adequate as evidenced by new belts and rollers at critical sections of the conveyor transport system and by the results of the mechanical/electrical operability tests. Thus while the main mining equipment may be in relatively good condition mechanically and electrically, the mines are in very poor condition from a mining operations point of view. The amount of coal uncovered and readily available for extraction is limited to 1-2 months. The overburden removal apparently has been neglected over the years. As a result, the mining fronts are steep and unstable. Presently, mine operations are hampered by several landslides at the benches for overburden excavators, in particular in the Bardh mine. It is very doubtful whether the slides could be removed during the winter to achieve the normally required bench advance to uncover more coal. There is a risk that additional slides may occur. Furthermore, at the southern sidewall of this mine, an important overburden conveyor is

threatened by the burning (smoldering) of coal remnants, caused through self ignition of the coal. Also, less critically for mining, but disturbing from the environmental point of view, there are several smoldering fires of coal remnants in the dumped overburden. Insufficient water drainage on some benches is another impediment to production. Poor access road conditions may also hamper machine maintenance and operation in wet weather. In general, the mines show very poor housekeeping. All these visible indicators point to negligent operational and managerial practices that have been maintained over years and will be very difficult to change. They are a threat to sustainable and efficient operation. The main concern is the insufficient speed of overburden removal despite the low capacity utilization of the mines over the last 10 years. It is likely that there is a serious problem of poor machine utilization and inefficient mine management.

20. In July 1999, the mines restarted production at a rate of about 200,000 tons per month. Despite the low level of production, there is presently a stock of 550,000 tons of coal available at the power plants. The total storage capacity is 700,000 tons. The high level of stocks indicates that the mines have been able to meet the reduced power plant demand, despite the lack of auxiliary and mobile equipment and despite the frequent power outages and inability to restart the mining equipment due to the low voltage supplied by the power plants.

District Heating

21. In general, the DH systems appear to have suffered only minor conflict damage. However, in all cities, damage due to lack of maintenance has been significant. The DH system in Prishtine is over 25 years old and recognized to be relatively inefficient. The main causes are the use of a constant-flow variable-temperature system with no temperature control or metering at the user end, and the use of technology that leads to a low life expectancy and high heat losses. Water losses were about 20 percent in 1998/99, due in large part to lack of maintenance.

Environment

22. Pollution resulting from power generation, district heating and associated coal mining is prevalent in the area around Prishtine. Estimates from the late 1980s for particulate emissions are on the order of 80,000 tons a years and for sulfur dioxide some 50,000 tons a year from both power generation and district heating – which exceeds WHO guidelines. Although Kosovo B is equipped with precipitators, it is not clear if these units were used during recent operation before shut down. In any case, these precipitators and the water treatment system need to be refurbished and updated. For the district heating plant, pollution mainly results from the poor quality of heavy fuel oil – and it is likely that only very little can be done short of replacing the plant in its entirety as well as major sections of the distribution systems.

Current Situation – Institutional Issues

23. Presently, there is no adequate institutional framework for efficient operation of either the power and DH systems or the coal mines. There is no company structure and no business culture, and no functioning billing and collection service. Proper records and planning tools are missing. The previous higher-level managers have left, leaving a vacuum at the top. Most of these positions have been filled with Kosovar Albanians, but many have insufficient experience.

24. In this situation, UNMIK moved quickly to install a committee for the supervision of the power system and mine operations, and entrusted the management to KFOR. While this may have been the only practical immediate solution, it is not a sustainable arrangement and should be

changed as soon as possible. Senior local managers are trying to create a new corporation, Kosovo Electricity Corporation (KEK), unifying the mines, power plants, transmission and distribution. However, the corporation has no legal status as of yet. Fortunately, it appears that the sector is staffed with experienced personnel at the lower and middle levels of management and that there is no significant shortage of skilled technicians and operators. This should facilitate resumption of normal operations of the system provided an appropriate institutional framework can be established, with concurrent arrangements for the provision of advice and training for the senior Kosovar managers. A contract has been recently awarded to a British firm to assist in the management of the operations during the 1999-2000 winter.

Current Situation – Policy Issues

25. In view of the complex political and legal issues that have yet to be resolved for Kosovo as a whole, it would be premature to attempt to define what the future structure of the energy sector should be. Once progress has been made in resolving these issues, the legal and regulatory framework for the sector can be defined. However, there are a number of policy challenges related to the operation of the energy sector and these are described in the following paragraphs.

26. ***Organizational Issues.*** There are indications that the local population does not feel part of the current process of identifying and implementing the measures needed for sustainable development of the Kosovo energy sector. This could develop into a major issue and needs to be carefully addressed. There is also an important issue regarding the future organizational status of the coal mines as to whether they should be part of the power utility or under separate management.

27. ***Human Resources Issues.*** The limited availability of managerial expertise and experience has to be addressed, by making available appropriate advisory services and by training. There is also a need for a labor policy governing employment terms and conditions, as well as the statutes of labor unions.

28. ***Improving Sector Finances.*** At present, there is no billing for electricity consumption and therefore no cost recovery. Similar issues will arise when the district heating systems become operational in October. There is a need to put in place a modern financial management system, and to recruit and train staff to work with this system.

29. ***Environmental Aspects.*** There have been poor environmental practices in the past, particularly in the context of the power plants and coal mines. It is essential that proper environmental policies be in place and effective enforcement practices be followed.

B. SECTORAL PRIORITIES FOR RECOVERY

Objectives

30. ***Short-term Objectives (covering the period to spring 2000).*** The short-term objectives for the energy sector in Kosovo have to be the provision of acceptable levels of service (supply of electricity and, where applicable, of district heating) during the coming winter and initiation of measures linked to cost recovery and institution building.

31. Provision of an acceptable level of service in the energy sector during the coming winter poses an immense challenge, and could be one of the most critical aspects affecting the credibility of UNMIK and the donor community. In order to provide such levels of service, immediate and

sustained actions are required to address the wide range of issues confronting this sector. Failure to do so could result in a significant segment of the population having to face, at the very least, considerable hardship during the winter. The issues to be addressed are, for the most part, well known. The options available are limited. What is needed is a mechanism for quick decision-making, arranging the necessary financing, and putting in place appropriate implementation mechanisms. Normal procurement and other administrative procedures will largely have to be bypassed for this winter.

32. The estimates of the projected peak demand for the coming winter vary widely, ranging from about 500 MW to over 1,000 MW, compared to a summer peak demand of about 300 MW, a significant part of which was met by imports from Albania and Serbia. This demand could be constrained by the inability to rehabilitate a major part of the damaged distribution network prior to the winter. Based on available data, it is estimated that a peak demand of about 600 MW would be a reasonable figure to adopt for planning purposes. At the same time, appropriate load-shedding measures should be planned to manage excessive demand and/or shortfalls in domestic generation or electricity imports.

33. During the winter, Serbia and Albania (as well as the Former Yugoslav Republic of Macedonia) will also be short of electricity and therefore are unlikely to be able to supply electricity to Kosovo. Although efforts can and should be made to reach an agreement with Greece (which does have a surplus in winter) for import of electricity, the quantity likely to be available from this source does not affect the strategy to be adopted for meeting the estimated demand.

34. This strategy has to be based on preparing both units of the Kosovo B thermal power plant for operation, and taking measures to improve the likelihood that both the Kosovo A thermal power plant and the Gazivode hydropower plant are capable of being operated at reasonable levels. If this is achieved, about 600 MW can be available domestically, although the supply from Kosovo A may be unreliable. The balance demand, if any, would have to be met from imports and/or by load-shedding. If arrangements for significant imports can be made, the production from Kosovo A can be reduced appropriately. For next winter (2000-2001), both units of Kosovo B and one unit of Kosovo A would have to undergo major overhauling during the summer. The objective of the overhauling would be to enable the Kosovo B plant to function as the primary source of domestic power for the next 15 years, and the Kosovo A unit to be able to meet the residual demand for another 3 to 4 years until replacement generation capacity is installed. If reliable long-term electricity import arrangements can be made, overhaul of the Kosovo A unit may not be required.

35. Concurrently, urgent rehabilitation of the transmission and distribution networks has to be carried out to transmit and distribute the electricity to meet the projected demand. Initial reconstruction efforts should target mainly principal substations, major transmission lines, and distribution networks.

36. The capability of the coal mines of Mirage and Bardh to produce the quantity of coal required for use as fuel for the Kosovo A and B thermal power plants, and for meeting the limited requirements of domestic consumption, has to be ensured.

37. Ensuring satisfactory operation during the winter of the district heating systems in the cities of Prishtine, Gjakova and Mitrovica is essential not only from the point of view of providing a critical service but also from some of the consequences of a failure to do so. This would result in the district heating customers switching to electricity for space heating and could

add an additional 150 MW to the electricity demand. Domestic generating capacity is already limited and it is unlikely that this additional demand can be met by imports. Even if this demand could be met, it would lead to overloading of the distribution system. Consequently, the systems in Prishtine, Gjakova and Mitrovica have to be brought into operation for the coming heating season. An exception is the DH system in Lipljan, which has been out of service for eight years and can no longer be considered operational. Critical is the supply of mazut, which will have to be provided via the Former Yugoslav Republic of Macedonia.

38. Measures necessary to initiate progress towards cost recovery have to be given priority. These include restoration of the billing and collection activities, procurement and installation of meters (estimated requirement: 150,000 meters), analysis and control of cost of services, and review of tariff structures.

39. In the short-term, a balance has also to be struck between environmental concerns and the need to restart urgently some of the most polluting installations. But beyond the emergency period, measures should be taken to mitigate environmental risks. A detailed environmental assessment is needed, to assess the situation, determine the main causes of pollution, identify options for remedies, and propose least-cost solutions. In addition, the environmental monitoring capability that existed during the 1980s should be replaced, so as to provide the means for a proper control of pollution levels.

40. Interim institutional arrangements will have to gradually give way to more permanent arrangements with greater local participation. Defining and developing these more permanent institutional arrangements will require careful consideration of a number of complex issues.

41. ***Medium-term Objectives (covering the period from spring 2000 to spring 2003).*** In the medium-term, the objectives have to be expanded to include all aspects necessary for full reconstruction and sustainable development of the energy sector. To achieve these objectives, it will be necessary to undertake comprehensive efforts to collect required data and analyze available options before developing the detailed measures to be implemented to achieve these objectives. These efforts should be undertaken with maximum local participation.

42. One of the primary medium-term objectives has to be the resolution of legal and other issues relating to the establishment of a power utility. This is of critical importance for the successful development and implementation of measures necessary for sustainable development of the energy sector.

43. Wide-ranging studies to define the future physical investment needs of the power sub-sector will be required. These will include: a least-cost generation expansion study to define future generation capacity requirements and analyze various options of providing it; feasibility studies for upgrading the dispatch center and establishing a SCADA system; and developing a masterplan of the transmission and distribution networks. These studies will identify the additional investment needs. Other studies related to the future structure of the Kosovo power sub-sector, regulatory issues, etc. can be undertaken once related legal and ownership issues have been resolved.

44. Establishment of a computerized financial management system based on International Accounting Standards will also be a priority. Services of an accounting and auditing firm will be required to establish a financial management system, preferably common to both the power utility and the coal mines. The objective will be to develop a local financial management capability to produce reliable and transparent cost reports in line with International Accounting Standards, and

to execute efficiently all financial transactions required for an autonomous enterprise established on the principles of cost recovery. Depending on the qualifications and performance of the firm, it would be desirable that the firm, after its initial intervention, continues to provide training as needed and carries out financial audits of the power generation and mining operations.

45. For the coal mines, the key objective is to establish sustainable coal supply to the power plants at quantities and costs compatible with the requirements of competitive marketing of electricity in the domestic market. An operational audit is needed as soon as possible to identify managerial/organizational changes required to correct past negligence and enable efficient future production, to assess the technical capability of existing equipment to provide sustainable production in line with power plant consumption, and to identify the additional investments needed.

46. As a basis for improved mine and environmental planning, the mines should be surveyed from the air and new maps should be prepared. This is a task that would be executed by a specialized firm after completion of the operational audit, under terms of reference prepared by the auditing team.

47. The main heating system in Prishtine is more than 25 years old and inefficient. For the medium-term, and in order to justify investments in extensive rehabilitation of heating systems in Prishtine and other cities, a feasibility study needs to be carried out. The study will examine different options for supplying heat, and possibly hot water and electric power, to consumers and recommend the least-cost solution.

48. In the medium-term, new precipitators are probably needed at the power plant to mitigate environmental risks. Such a major investment should, however, be financed only in the framework of a medium-term development strategy for the energy sector, and on the basis of an environmental audit.

49. **Recovery Program Measures.** The measures to be taken for the Energy Sector Recovery Program have been identified for each of three phases: Phase 1, covering the urgent needs of the period up to December 2000; Phase 2, covering the following twelve months (April 2000 to December 2000) where the efforts will be directed at continuing rehabilitation and initiating actions for the medium-term; and Phase 3, covering the measures to be undertaken during the following three years (to 2003) towards achieving sustainable development. Action on several of the measures listed under Phase 1 is already being taken.

50. **Financing Requirements.** A critical element in the timely undertaking of the measures listed below will be the availability of sufficient financing. Table 1 provides a preliminary estimate of the financing requirements of the sector over these three phases. A number of donors have already indicated their willingness to finance some of the urgent investment needs outlined in Table 1. These include EC and SIDA for power generation; DANIDA, DFID and Norway for power transmission; DANIDA and EC for dispatching; DANIDA, DFID, France and GORED for power distribution; EC and Netherlands for the coal mines; and EC for salaries.

51. **Implementation.** Implementation of the Recovery Program for the energy sector will be a major and complex undertaking, which will require coordinated and sustained efforts on the part of all the entities involved in the sector. The role and responsibility of each entity will have to be clearly defined, and effective local participation will have to be maximized. The adoption of appropriate fast-track procurement procedures will be an essential requirement for successful implementation, particularly for the measures to be undertaken for Phases 1 and 2.

Physical Investment

52. Substantial investments are required for the physical rehabilitation of the energy sector in Kosovo. These requirements are outlined, together with indicative costs. The cost estimates are very preliminary and have been prepared to give an order of magnitude of the need for external financing. In particular, the Phase 3 investments will depend entirely on the outcome of the studies to be carried out in Phase 2. Some of the cost estimates are based on the Report on "Energy Sector Priority Programme – Winter 1999/2000" prepared by the International Management Group for the European Commission.

Power Generation

- Essential repair and maintenance of the two units of the Kosovo B thermal power plant (including the balance payment to the manufacturer for the supply of a complete LP rotor which was ordered pre-conflict and is ready for delivery) in order to permit earliest possible operation of both units as the primary source of domestic power generation during the coming winter (Phase 1)
- Major overhaul of the two units of the Kosovo B thermal power plant. The contract has to be awarded by November 1999 (Phase 1) to enable the overhaul to be carried out during the summer of 2000 (Phase 2).
- Rehabilitation of one unit of the Kosovo A thermal power plant to enable the unit to continue to function for another three to four years until replacement generation capacity has been provided. The contract has to be awarded in Phase 1 to enable the rehabilitation to be carried out during the summer of 2000 (Phase 2).
- Provision of additional generation capacity (200 to 250 MW) to replace the Kosovo A thermal power plant (Phase 3).

Power Transmission

- Rehabilitation of identified critical segments of the 220 kV and 110 kV transmission lines and identified substations (Phase 1).
- Rehabilitation of identified segments of the 400/220/110 kV transmission lines and identified substations (Phase 2).
- Reinforcement and expansion of the transmission network on the basis of the results of the master-planning study (Phase 3).

Power Distribution

- Rehabilitation of identified segments of the distribution network (Phase 1).
- Assign priority to de-mining operations in those areas where rehabilitation of the distribution network is held up because of mines (Phase 1).
- Procurement of 50,000 meters and installation (order in Phase 1, install in Phase 2).
- Rehabilitation of the remaining damaged segments of the distribution network (Phase 2).

- Reinforcement and expansion of the distribution network on the basis of the results of the master-planning study (Phase 3).
- Procurement of 100,000 meters and installation (Phase 3).

Coal Mining

- Purchase/lease of bulldozers and other auxiliary equipment needed to remove slipped overburden in critical areas, to enable the moving of conveyors, drainage of water from some benches and access to equipment in wet weather (Phase 1).
- Purchase of auxiliary equipment and rehabilitation/overhaul of major mining equipment (Phase 3).

District Heating

- Essential replacement/repairs for boiler tubes, network piping, heat exchangers and pumps (Phase 1 and Phase 2).
- Major rehabilitation/replacement of the district heating system on the basis of the results of the feasibility study (Phase 3).

Environment

- Conduct an environmental audit on the power generation facilities (Phase 1).
- Restore air quality monitoring equipment in Prishtine (Phase 2).
- Rehabilitate / replace precipitators and possibly other equipment at the power plants (Phase 3).

Operating Costs Financing

53. The financing requirements for the energy sector will have to include, at least for Phases 1 and 2, a provision for financing operating costs. Given the difficult post-conflict conditions and the lack of pre-conflict data that could be used for forecasting the likely performance on billing and collections, only preliminary estimates can be made of these requirements. As electricity billing is expected to commence in January 2000, revenue collection during Phase 1 will be nominal and almost all operating costs for the coal mines and the power sub-sector will have to be financed from external sources, including arrears of salaries of staff. For Phase 2, an average subsidy of US\$1 million per month for salaries has been included in the financing requirements. It has been assumed that revenues will be sufficient to cover operating costs other than salaries in Phase 2, and all operating costs in Phase 3. These assumptions will need to be continuously reviewed as experience is gained with actual billing and collections.

54. For district heating, the major operating cost is that of mazut. Salary costs are comparatively not significant. For the Prishtine district heating system, the pre-conflict staff strength was about 160 and currently is less than half of that. For Phase 1, the operating costs for mazut, essential spare parts and necessary repairs have been included in the external financing

requirements. It has been assumed that operating costs for subsequent phases will be covered by a combination of collection of DH bills based on revised tariffs and subsidies from taxes collected by the municipalities, the latter source being the pre-conflict arrangement. Efforts will have to be made to achieve a rapid reduction in dependence on subsidies.

55. Operating costs other than salaries are listed as follows:

Power Generation

- Procurement of essential spare parts, consumables, and tools for the Kosovo A and B thermal power plants (Phase 1).
- Procurement of essential spare parts and tools for the Gazivode hydropower plant, and arrange for necessary repairs (Phase 1).
- Procurement of mazut, diesel and chemicals required for the operation of the thermal power plants (Phase 1).

Import of Electricity

- Negotiate, finalize and sign agreement(s) for the import of electricity during the coming winter (estimated cost unknown, partly offset by fuel savings).

Power Transmission

- Procurement of essential spare parts, consumables, and tools for the transmission network (Phase 1).

Power Distribution

- Procurement of essential spare parts, consumables, and tools for the distribution network (Phase 1).

Coal Mining

- Procurement of essential spare parts, tools, safety items, fuels and lubricants (Phase 1).
- Arrange for necessary repairs to the coal transport system (US\$0.1 million, Phase 1).

District Heating

- Make necessary arrangements for the import of fuel (mazut), which was previously obtained through Serbia (Phase 1).
- Procurement of essential spare parts, and arrange for necessary repairs (Phase 1).

Institutional Requirements

56. The following measures related to institutional requirements are to be undertaken:

- Clarify issues related to the role, authority and responsibility of KEK (Kosovo Electricity Corporation) and other entities involved in the functioning of the power sector (Phases 1 and 2).
- Award contract for management and technical assistance to be provided to KEK to assist it in operating the power sector (including the coal mines) in such a manner as to provide reliable power supply during the winter, ensuring that the assistance is provided by competent professional staff (Phase 1).
- Develop and implement an effective mechanism for billing electricity consumers (both those with functional meters and those without) and collecting the payment for these bills (Phase 1).
- Design appropriate load-shedding measures to manage excessive demand and/or shortfalls in domestic generation or electricity imports, taking into account security and other considerations (Phase 1).
- Initiate formal dialogue with the power entities of neighboring countries to improve cooperation on issues related to a more stable operating regime for the power network of the region (Phase 1).
- Arrange for a comprehensive study of the future needs of the power sub-sector including a least-cost generation expansion study; feasibility studies for the upgrading of the dispatch center and establishment of a SCADA system; and developing a masterplan of the transmission and distribution networks; and identifying additional investment needs (Phase 2; but with the contract being awarded by the end of Phase 1).
- Establish a computerized financial management system according to International Accounting Standards (Phases 2 and 3; but with the contract being awarded at the end of Phase 1).
- Arrange for required advisory services and training (Phases 1, 2 and 3).
- Arrange for an operational audit of the coal mines to identify potential organizational and management improvements, review adequacy of existing equipment to meet projected production targets, and identify additional investment needs (Phase 1).
- Arrange for aerial mapping of the mines (Phase 1).
- Arrange for a feasibility study of the future district heating needs and of the various options to provide this service, and identify future investment needs (Phase 1).

Policy Requirements

57. The following are the preferred options for dealing with the sectoral policy challenges defined earlier.

58. ***Organizational Issues.*** There has to be ownership of the Recovery Program by the Kosovars, as well as effective participation by them in the implementation of the program. Without such ownership and participation, the interim arrangement cannot effectively undertake the immense task of operating the coal mines and the power and district heating systems to

provide satisfactory levels of service during the winter. Furthermore, the longer-term implications of a failure to involve them could be significant. It is therefore important that issues related to the legal status and the role of the Kosovo Electricity Corporation (KEK), and of other entities involved in the functioning of the power sector, be clarified expeditiously. The coal mines could be run as a department of the power utility, as a profit center or as a subsidiary company. In the latter two cases, a lignite price would have to be agreed and supply conditions would have to be spelled out. While this is normally preferred for reasons of motivation, transparency and efficiency, it is not a recommended solution in this case, at least not in the short run. There is little prospect for the mines of selling lignite outside the power plant supplies. There is also scarce expertise for business management of large industrial enterprises and it appears preferable to concentrate it in one entity, uniting the power utility and the coal production. Issues related to the management of the district heating entities and their efficient supervision by the municipalities also have to be addressed.

59. ***Human Resources Issues.*** The limited availability of managerial expertise and experience has to be addressed by a comprehensive program of technical assistance and training. There is also an urgent need for a new labor policy which provides guidelines for recruitment and dismissal, negotiation of labor contracts, the rights and duties of labor unions and the payment of wages and eventually other benefits. Ideally, this policy should be valid for all employment within Kosovo. If potential legal and political problems preclude a new comprehensive labor policy, temporary guidelines should be issued. It is important that such guidelines do not establish permanent rights for work and benefits, that they deal carefully with the issue of wage arrears, and that payments to miners and workers in the energy sector are not substantially higher than those for other industrial workers. It is also essential to prevent the build-up of surplus labor, as this would become a major obstacle to the efficient operation of the sector.

60. ***Improving Sector Finances.*** Any prolonged supply of free services makes subsequent collection efforts much more difficult. There is thus an urgent need to restore billing and collection functions as soon as possible, in parallel with an emergency program to install meters. Concurrently, analysis and control of cost of services has to be undertaken, and tariff structures reviewed. Based on this analysis, a program for achieving full cost recovery in a reasonable period of time has to be developed. Similar measures are required for the DH systems. Another important related measure required will be appropriate arrangements to facilitate payment of bills by consumers.

C. COST ESTIMATES

61. The following cost estimates are very preliminary estimates prepared to indicate the extent of the need for external financing. In particular, the Phase 3 investments will depend on the outcome of the studies to be carried out in Phase 2.

**Table 1: External Financing Requirements for the Energy Sector
(in millions of US dollars)**

Activity ¹	First Phase (until December 2000)			Second Phase (2001-2003)	Total
	Until March 2000	April to Dec. 2000	Total		
INVESTMENTS					
Kosovo B	6.6	25.0	31.6	0.0	31.6
Kosovo A	1.2	20.0	21.2	0.0	21.2
Other Generation	5.3	0.0	5.3	150.0	155.3
Transmission	2.2	5.0	7.2	20.0	27.2
Distribution Network	16.6	10.0	26.6	30.0	56.6
Metering	5.0	0.0	5.0	10.0	15.0
Coal Mines	5.9	1.9	7.8	10.0	17.8
District Heating	7.3	4.0	11.3	30.0	41.3
Environment	0.0	2.0	2.0	29.0	31.0
Subtotal	50.1	67.9	118.0	279.0	397.0
TECHNICAL ASSISTANCE					
Management Contract	0.0	1.4	1.4	0.0	1.4
Study of Power Sub-sector	0.0	5.0	5.0	0.0	5.0
Financial Management System	0.0	1.5	1.5	1.4	3.0
Advisory Services & Training	0.6	0.6	1.2	1.0	2.2
Coal Mine Audit & Mapping	0.5	0.0	0.5	0.0	0.5
District Heating Study	0.0	1.0	1.0	0.0	1.0
Subtotal	1.1	9.5	10.6	2.4	13.0
Total²	51.2	77.4	128.6	281.4	410.0

¹ Commitments have recently been made for some of the activities listed in this table.

² In addition, about US\$40 million will have to be funded through the budget for operating expenditures in the sector.

ANNEX X: TRANSPORT

I. ROAD SECTOR

A. ROAD SECTOR DESCRIPTION

Description of the Road Sector in 1989

1. The road network of Kosovo consists of about 3,800 kilometers of roads, including 623 kilometers of main roads, and 1,300 kilometers of regional roads. Network density is relatively low, at about 0.35km/km². Adequate development and maintenance of the road network in Kosovo has been an issue which has been worked on since the 1970s.¹ While the road network has been developed, road maintenance has been persistently under-funded. This has resulted in a continuous deterioration of the road network.

2. Until 1989, physical planning and administration of the main and regional road networks were handled principally by a provincial Road Organization, staffed with about 550 employees, and headed by a Board whose members represented various groups having an interest in roads. The Federal Government (Socialist Federal Republic of Yugoslavia – SFRY) played a role limited to common policy and regulatory matters, such as control of vehicle weight and dimensions, road safety and international aspects. Local roads were under the jurisdiction of local communities which had special departments for this purpose. Following the end of provincial autonomy in 1989, and until June 1999, the management of the Road Organization was changed from Kosovar Albanians to mostly Serb Kosovar staff. During this period, resources allocated to the rehabilitation and maintenance were limited, and, most probably, non-existent during the conflict.

Current Situation

3. Most of the road network is by now serviceable – but at a low standard – and there is urgent need for rehabilitation on about 25 percent of the main and regional road networks. In addition, a study on future road traffic in Kosovo needs to be carried out to assess whether the capacity of the main network needs to be increased (based on preliminary estimates, current traffic on the main network does not seem to exceed 5,000 to 6,000 vehicles per day).

Damage to the Road Network

4. Damage observed on the road network (generally potholes, cracks and water running on the road surfaces) results primarily from a pervasive lack of adequate maintenance over an extended period of time. Damage is most severe on roads which were under the responsibility of municipalities, including parts of the main and regional roads going through the municipality and local roads. In a number of cities, some sections of the main network have deteriorated to the point that vehicles actually drive on the road sub-base. Direct damage resulting from the conflict is limited to a few shell and bomb craters.

¹ In 1986, the budget of the Kosovo Road Organization was about US\$16.7 million, which was divided almost equally between rehabilitation, maintenance and debt servicing.

5. Thirteen bridges were damaged during the conflict: (i) six of them are temporarily replaced by one-lane steel bridges installed by KFOR; there remain, however, severe traffic jams at the crossing of these bridges with waiting time frequently exceeding one hour. This hampers traffic on Kosovo's two main axes, (Prishtine – Peja and Prishtine – Mitrovica) In addition, KFOR has announced its intention to withdraw the temporary bridges before next summer, and reconstruction should therefore take place as early as possible; (ii) bypasses are in place for four other destroyed bridges; and (iii) the three remaining damaged bridges have suffered relatively less damage and can be used, at least in the short-term. All bridges on the main and regional road networks which have not suffered direct conflict-related damage seem to be in fair condition, despite the lack of maintenance and relatively poor design.

6. Since the beginning of the conflict, shifts in traffic composition and frequency have been observed. For example, the road network has been used by heavier vehicles than in the past, including KFOR vehicles and transit traffic-- most of which have an axle load above the standard 10-tons axle load limit used in road design in Kosovo. The new traffic composition puts an extra burden on already exhausted road structures, as well as on networks under the roads such as water and sewage systems. In addition, there has been much more traffic on certain local roads due to persons having sought shelter in mountainous areas. A number of gravel and dirt roads have been over-used and as a result, have numerous potholes. Finally, over the years, most of the horizontal and vertical signalization has disappeared.

Road Organization Status

7. Following the departure of Serb Kosovar staff, the Road Organization was re-staffed spontaneously in June 1999 by Kosovar Albanians, some of whom were part of the staff prior to 1989. However, the Road Organization as proposed by the now Kosovar Albanian management, has not yet been recognized officially nor integrated in any institutional structure. Staff of the present Road Organization work with almost no resources.

Road/Bridge Construction and Maintenance Capacity

8. There are four main construction and maintenance companies located in Kosovo. They are able to undertake road maintenance and rehabilitation works. They can also undertake light rehabilitation works on bridges. Staff is available to restart working. However, these companies have lost part of their construction and maintenance equipment, which constrains their capacity at present.

B. ROAD SECTOR PRIORITIES FOR RECOVERY

Objectives

9. The objectives of the road rehabilitation program are as follows:

- Ensuring that the serviceability of the road network remains as high as possible throughout the 1999-2000 winter. Required activities include: winter maintenance; temporary fixing of the most damaged parts of the main road network; winterization of temporary bypasses; and emergency repairs on an ad hoc basis, following landslides, pavement breakups and the like. KFOR has indicated that it will carry out winter maintenance on the theater routes, and on those parts of the regional network used for troop movements and for humanitarian aid purposes. Local companies, if provided with equipment, salt and sand, will be able to complement KFOR actions.

- Carrying out the rehabilitation of the road sector over a period of about 3 years and establishing adequate construction/maintenance capacity. The objective is to support local companies in restarting their operations by maximizing their involvement in the rehabilitation of the road sector. To achieve this objective, a two-tier approach is proposed: (i) using as much as possible local capacity to implement the program: (a) on the main and regional networks, rehabilitation contracts sized to meet the capacities of these companies; and (b) on the local network, use of labor-intensive methods to upgrade gravel and dirt roads; and (ii) provide essential equipment to those companies which can prove to be viable, and in need of such equipment. Special attention should be paid to ensure adequate supply of asphalt and concrete. The proposed program therefore includes the provision of spare parts to rehabilitate existing plants.
- Creating an efficient road administration. The objective is to determine the functions and adequate size of the Road Organization, provide the equipment necessary for its operation, and to bring its staff up to date on the latest technologies and management techniques.
- One important question which involves road investments but which does not fall under road planning and administration as such, is the question of the arrangements of the border crossing at the Former Yugoslav Republic of Macedonia border. There are significant delays for traffic in both directions, caused by the functioning and lay-out of the border area, including roads and parking areas, which have to be improved. This should therefore receive the highest priority, once the necessary agreements have been reached and design prepared. Generally, the traffic jams which can be observed around Prishtine and other places, such as markets etc., is a problem to be resolved primarily through traffic management and involvement of traffic police.

Physical Investment

10. It has been estimated that, in a first phase, rehabilitation works will need to be carried out on about: (i) 450 kilometers of road sections, mostly located on the main network. Rehabilitation works include patching, overlays, reconstruction, and drainage works; and (ii) 400 kilometers of gravel and earth roads, using labor-intensive work methods. In addition, all of the damaged bridges are proposed to be reconstructed in a permanent fashion. Finally, equipment will need to be provided as follows:

- Winter maintenance equipment: this equipment needs to be provided on an emergency basis to help local contractors to keep open the part of the network not under KFOR supervision. This is especially important in order to allow transport of humanitarian aid to remote places. Equipment includes mainly snowploughs, trucks, and salt spreaders. In addition, about 2,000 tons of salt and 2,000 tons of sand will need to be supplied.
- Road maintenance equipment: basic road maintenance equipment is required in order for the companies to be able to restart operation on a significant scale. Equipment includes mostly trucks, earth and overlay works equipment, as well as spare parts for asphalt plants and crushing units.
- Horizontal and vertical signalization: marking equipment is needed in order to restore horizontal signalization, especially continuous and stop lines, as well as pedestrian crossings. In addition, vertical signalization is needed on most of the network. As no comprehensive assessment of the needs in vertical signalization has been undertaken so

far, it is proposed that a donor finances both the assessment and the equipment, once the assessed needs have been agreed upon with the Road Organization.

11. In order to help with the likely cash shortage that Kosovo will be facing in the near future, it is proposed that donors make in-kind road equipment donations to UNMIK, which in turn will give it to contractors as a mean of payment against activities carried out under the road maintenance and rehabilitation program.

12. With respect to rehabilitation of local roads, it is proposed to carry out the works by maximizing use of labor, using unemployed persons with shovels and wheelbarrows to fill the potholes, and clean/create drainage systems. This component could be supported by donors with in-cash contributions to pay the workers. The administration of the contracts could be carried out through the PIU, which would advise local contractors on setting up teams of workers and on implementation issues.

13. The Road Organization would need to be provided with training and basic office and communication equipment, in order to restart activities on a full scale. Donors are also encouraged to provide for twinning arrangements between the Kosovo Road Organization and their own road administrations.

Operating Cost Financing

14. Over the next 4- 5 years, it is estimated that at least US\$8 million will need to be spent each year on the main and regional road network in order to ensure a more adequate level of maintenance. As the budget of Kosovo will be unable to provide sufficient funds to cover road maintenance at least for the next year, donors are invited to support road maintenance activities through cash contributions, supply of bitumen or of road equipment. It is expected that the Road Organization will be linked to UNMIK, which could provide for part of the recurrent costs.

Institutional Requirements

15. It is clear that the Road Organization was overstaffed with over 500 employees in the past. The actual number and skill mix of staff now required to optimize the efficiency of the Road Organization is unknown. It is thus recommended that the Road Organization be staffed with no more than 100 staff for the time being. The PIU should be asked to conduct a study to propose an optimal organizational structure based on economic efficiency. The study should also formulate precise recommendations with respect to the maintenance prioritization process, set up of a pavement and bridge management system, and training to be provided to the Road Organization staff, as well as questions relating to the functioning and capacity of the contracting industry.

Policy Requirements

16. The main policy issue is the financing of road maintenance activities. This can be done through ear-marking of portions of specific revenues (usually fuel taxes, registration fees and the like) or through annual allocations from a general budget. None of the two mechanisms has proven safe enough to fully guarantee that sufficient funds be allocated to maintenance, as allocations of budget resources, is ultimately a political decision. However, it is recommended that UNMIK start as soon as possible to collect revenues and to take into account maintenance requirements in the preparation of budgets. Other issues include: (i) creation of a traffic police force for traffic and safety management; (ii) issuance of car licenses and re-establishment of

regular technical controls of vehicles; (iii) monitor axle loads on the network; and (iv) re-establishment of the Statutes of the Road Organization.

II. RAILWAYS

A. RAILWAY SECTOR DESCRIPTION

Description of the Railway Sector in 1989

17. The railway network in Kosovo consists of 330 km of single track, non-electrified standard gauge route length. Much of this is in relatively mountainous terrain with steep slopes and sharp curves. The network consists essentially of two lines, one north-south and one east-west which cross at Kosovo-Polje, and one branch line between Klina and Prizren. The north to south line, which connects to Kraljevo (and Belgrade) in the north and Skopje in the south, has been the most important line which has served as an alternative to the main line Belgrade-Nis-Skopje. There are also numerous industrial sidings.

18. In the 1980s, the rail traffic was about 3 million tons of freight. Most of this was bulk commodities needed for or produced by the mining, metallurgical and chemical industry. Passenger traffic was about 4 million passengers, mainly over short distances. About 2500 staff were employed. Financial problems and the need for hefty subsidies have been a permanent characteristic of the system.

Current Situation

19. Traffic on the lines to Peja and Prizreni ceased in early 1998 because of security concerns. On the line to Podujeva, traffic has been discontinued since a number of years. The section between Kosovo Polje and the airport suffered heavy damage during the conflict. In June, KFOR re-established traffic between Prishtine and Volkovo (at the border with the Former Yugoslav Republic of Macedonia) where it now runs on the average four pairs of trains daily, for KFOR and humanitarian supply needs. There is also some service between Prishtine and Mitrovica. KFOR is currently operating the railway infrastructure for its own needs, and intends to maintain control over the network until March 2000, and to transfer it to full civilian operations by September 2000. A civil management team has been appointed by UNMIK for a period of seven months to support the KFOR regiment. This team will be responsible, in particular, for training of local staff, for investments and donor coordination, and for the establishment of a commercial structure that is able to generate revenues. The team should also draft a strategic plan for the future development of the railways in Kosovo.

20. KFOR also intends to repair and extend the system to military requirements, under NATO funding, including: (i) a rehabilitation of the lines to Mitrovica, Peja and Prizreni; (ii) minor repairs on the main line's signaling system (including optics, glasses and cabling) to allow for a significant increase of capacity. Three locomotives are currently operational, and five additional locomotives will be needed in the short term to meet the needs. Depending on traffic development, the required number of locomotives should be reassessed.

B. RAILWAY SECTOR PRIORITIES FOR RECOVERY

Objectives

21. For the short run (up to September 2000), the railway operations will be under the responsibility of KFOR, with the investments needed on the infrastructure being financed mainly from NATO. An urgent investment, apparently not included, is the refurbishing and re-equipment of the workshop at Kosovo Polje which is needed for the operations. Presently the locomotives are being serviced under the open sky. With these investments, about 10-12 pairs of trains could be run on the line to the Former Yugoslav Republic of Macedonia, which is deemed to be sufficient for both military and humanitarian requirements. For the longer term, the future of the traffic development, and indeed of the railway as such in Kosovo, is dependent mainly on two factors:

- the situation in FRY, especially the opening of the line to Belgrade; and
- the future of the mining, metallurgical and heavy chemical industries in Kosovo.

22. While the railways have a potentially important role to play, until the above questions are clarified, no further railway investments should take place. When there is a reasonable overview of these questions, a study should be launched to determine what type of traffic is likely, with what requirements on what lines, and with what type of railway organization. Specifically, in the meantime, the railways should not employ and start paying the 1,250 nominal employees, but only those really needed for railway operations under prevailing conditions. This number, which is probably around 200, should, as a matter of urgency, be decided by UNMIK in consultation with KFOR and the present management, at the soonest. Whatever payments are needed to those persons not selected should be done through some social assistance mechanism. To do it through the railway would condemn it to permanent deficits, subsidies and inefficiencies.

Physical Investment

23. In the emergency phase, the workshop should be rehabilitated and equipped with the most needed tools. The loading/unloading ramp at Kosovo Polje should also be completed as soon as possible together with the adjacent freight areas in order to improve conditions. Fuel for the operations until Spring 2000 is also included. In the longer-term further investments should be decided only once the overall regional political situation is clearer.

Operating Cost Financing

24. It is assumed that the railways will not have on its payroll more staff than necessary, i.e., approximately 200. These staff could probably not be financed from the revenues generated, which is assumed to pay for fuel and other operating costs.

Institutional Requirements

25. The institution to run the railways exists in the form of the pre-conflict railway organization. This will have to be adapted to reflect the new conditions.

Policy Requirements

26. The policy should be to have a railway which is adapted to the demand for railway services, is managed commercially (non-politically), does not require subsidies, and does not employ more staff than needed. Extension of railway services should not be undertaken unless financially justified.

III. PUBLIC TRANSPORT

A. PUBLIC TRANSPORT SECTOR DESCRIPTION

Description of the Public Transport Sector in 1989

27. Public transport services used to be run in Kosovo by about 4,000 employees for a fleet of about 1,000 buses. Level of service was adequate but, like in many other places, urban transport services were run at a loss and their operations were supported through subsidies. At the beginning of the 1990s, the company in charge of public transport broke up, creating urban transport companies in the main cities as well as inter-city and international transport companies such as Kosovotrans Prishtine, a company with a fleet of about 100 buses and 250 employees. During the 1990s, operations, especially those of Kosovotrans, were limited by availability of fuel, new vehicles and spare parts. More recently, operations were severely affected by the conflict: buses were used for troop movements, stolen or burnt, and workshops were looted. However, some of the damage results from lack of adequate maintenance and investments over the last ten years.

Current Situation²

28. From the former Kosovo public transportation structure, it is estimated that about 3,600 employees are available to restart work, as well as about 30 buses owned by the former public transport companies, plus a number of privately owned buses. The buses available for urban transport operations are on average about 15 years old and appear totally worn out. For safety and environmental concerns, it is recommended to discontinue the use of these buses as soon as possible. In addition, workshops severely lack equipment and facilities and are no longer weather-proof. With respect to inter-city transport, available buses are on average 10 - 12 years old, and the level of maintenance performed on this fleet appears to have been higher than on the urban transport fleet. In the same way, workshops appear to be in better condition than those of the urban transport company.

29. However, it seems that demand for public transportation is met. Since the end of the conflict, the private sector has spontaneously filled the void created by the disruption of public transport services provision. In Prishtine only, it is estimated that between 150 and 200 small

² The findings related to condition of fleet and workshop are based on a quick survey of the public transport situation in Prishtine, which is the most important municipality of Kosovo. The situation might differ, but it is believed that Prishtine is representative for the purpose of this report.

buses and vans offer transportation within the city and its suburbs.³ In addition, it seems that up to 500 buses offer inter-city and international transportation services throughout Kosovo. These buses and vans are often owned by individuals who drive them for a living.

B. PUBLIC TRANSPORT SECTOR PRIORITIES FOR RECOVERY

Objectives

30. The situation in Kosovo offers a unique opportunity to dramatically improve the efficiency of the provision of urban transport services at minimal cost. The insufficiency of investment and maintenance over the last ten years, and the conflict have reduced the value of the passenger transport companies assets to almost nothing. In addition, the relationship between the companies and their employees has been cut off, as people left their employment during the conflict and the companies were not in a position to pay salaries. Thus, in the passenger transport field, the objective is to avoid re-creating the inefficient structures of the past, and to decrease the burden of passenger transport companies on public budgets, by: (i) ensuring sustainability of the provision of public services by the private sector; and (ii) complementing privately-provided services with publicly-provided services only if it can be demonstrated that privately-provided services fail to meet part of the demand.

Physical Investment

31. Although the situation in Prishtine does not warrant the support of the donor community, it is believed that there is a need to support the provision of urban transport services in smaller cities. It is thus proposed to supply 15 buses as well as some basic equipment to the urban transport companies. This will help maintain a minimum level of service, until it has been determined whether continuation of these companies can be justified on economic basis.

Operating Cost Financing

32. It is recommended that UNMIK contribution to salaries, if any, be limited to the strict minimum number of employees required to operate the number of buses operating now. Social support to former employees should be distributed through a channel separated from that of the company, in order to avoid confusion between social support and actual salary.

Institutional Requirements

33. A study should be undertaken in order to: (i) identify areas, if any, where public provision of passenger transportation is required; and (ii) propose a regulatory framework for the provision of passenger transportation by the private sector. This should include licensing arrangements, proposals on how to define a limited liability framework in which transportation companies could operate, and recommendations to public authorities on how to guarantee minimum service levels.

³ Before 1990, privately-owned small buses and vans were already used to complement urban transport services run by the public sector.

Policy Requirements

34. The policy requirements are as follows:
- (i) ensure a quick and full privatization of the inter-city and international passenger services providers which are publicly-owned;
 - (ii) support private provision of urban transport services as much as possible, which should lead to a progressive closure of the publicly-owned urban transport companies;
 - (iii) let market forces determine transportation prices, while ensuring that low income groups have access to passenger transport. This could be achieved by contributing from public revenues to the transportation costs. In order to minimize administration costs, this contribution could be built into the social support these social classes will be receiving; and
 - (iv) resolve across all sectors, the issue of compensation for involuntary termination of employment.

IV. CIVIL AVIATION

A. CIVIL AVIATION SECTOR DESCRIPTION

Description of the Civil Aviation Sector in 1989

35. In Kosovo there is one airport about 15 km south-west of Prishtine and four landing strips (length about 500 m) without relevance in this context. The Prishtine airport was built in the mid-1960s as a regional airport to be operated by mid-sized commercial aircraft, such as the B737. It was thus not designed to handle heavier wide-body aircraft, which were using Belgrade airport. The runway has a length of 2500 km, and the apron area is small, as is the terminal.

Current Situation

36. A British KFOR unit will operate the airport until June 2000. There is no Kosovo airport or civil aviation authority. There are only daylight operations (presently about 20 landings and take-offs per day) of both military and charter flights, but no regularly scheduled civilian services. There is a lack of ground lighting (40 percent of the runway lights are working) and limitations of the navigational aids.

37. There were damages to the airport during the conflict. The control tower and technical block were totally destroyed, the luggage reclaim area in the passenger terminal building was destroyed, and the pavements of the runways and taxiways received some relatively minor damage. The British unit has re-established daylight operations by:

- repairing runways and taxiways, and establishing temporary control tower radio communications and radar coverage;
- installing military navigational aids and emergency approach lighting, recommissioning the ILS (instrument landing system); and
- establishing rescue and fire fighting services, emergency power, refueling facilities and ground handling operations.

In addition, works have also started to weatherproof the passenger terminal, repair utilities and expand the cargo area.

B. CIVIL AVIATION SECTOR PRIORITIES FOR RECOVERY

Objectives

38. The objectives fall into two distinct categories. The emergency repairs are those which need to be undertaken immediately in order to reduce the very real possibility of having to close the airport during winter, which would impede delivery of most needed humanitarian aid to Kosovo. The investments beyond are intended to achieve a level which makes the airport operate under normal procedures and with a reasonable level of comfort for passengers.

Physical Investment

Urgent Investments

39. A longer term rehabilitation plan and its implementation will require a couple of years to be completed. In the meantime, there are urgent investments necessary to reduce the risk of disruption of air traffic. These urgent works are:

- (i) Aeronautical ground lighting (AGL). The existing lighting and cabling system is beyond repair and the control system has been destroyed. There is an urgent requirement for a new AGL system, compliant with the Standards and Recommended Practices of ICAO, together with a power ring main and standby generators. The floodlights at the parking apron also need replacing and additional floodlight masts installed.
- (ii) Navigational Aids. The ILS which has been recommissioned by KFOR, and is about 25 years old. The British unit operating the airport is very concerned about being able to keep it operational and have therefore urgently asked for its replacement.
- (iii) Pavement works. The surface has extensive cracking, and in many areas is close to disintegration. There is concern that in wet weather the surface friction will not be enough. The following works may be urgently required although this is subject to confirmation: treatment of joints and cracks in the surface; repair of distressed asphalt; and surface treatment of the runway and taxiway pavements to ensure an adequate level of surface friction.

40. In addition, a program of training of local staff to take over and run the airport operations (air traffic controllers meteorological services, miscellaneous other technicians) should get underway as soon as feasible.

Longer Term Investments

41. The Prishtine Airport has been brought into service by the military with temporary facilities. It is essential that preparation and design start for the permanent facilities which include:

- Permanent replacement of Control Tower and Technical Block;

- Cargo handling facilities;
- Passenger services;
- Equipment to replace the vehicles which have been loaned by the British, e.g. Rescue and Fire Fighting vehicles and Ramp Handling equipment;
- Maintenance facilities and workshops;
- Fuel storage and refueling facilities; and
- Power distribution and standby power for Passenger Terminal Area.

Implementation

42. By their very nature, the emergency investments should be done before this winter. This seems highly unlikely to happen if funding is to follow normal IFI or bilateral procedures. In fact, the only realistic arrangement appears to entrust the British Military unit, which is presently running the airport with this task by creating a fund of about US\$5 million to be put at their disposal. Responsibility for procurement, installation and operation of this equipment would rest with this unit, which could report to UNMIK and/or a qualified donor, depending on the source of funds. The longer-term program could be implemented in a more conventional way through UNMIK, and assisted by a unit appropriately qualified.

Operating Cost Financing

43. It is assumed that when the airport is handed back to civilian control and operations, civilian flights would provide sufficient revenues to cover salaries and other operating costs. Thus no special operating financing is foreseen.

Institutional Requirements

44. As the previous airport administration is, for all practical reasons non-existent, all the necessary staff will have to be trained, and a totally new organization will have to be created for the airport. This will involve both extensive training as well as, possibly, an external contractor to be responsible for the operation during some transitional period.

Policy Requirements

45. The airport company to be created should be a financially self-sustaining entity, managed independently from the government. Privatization should not be excluded as an option although this might be some time away.

Resumption of Civilian Scheduled Flights

46. Civilian flights can be resumed with the present equipment and requests to this effect have been forwarded to UNMIK. The operations would be under some restriction, mainly due to weather conditions, but would otherwise not represent any particular peculiarities. The financial benefits could be considerable, with estimates ranging at around 200,000 DEM/ month.

V. COST ESTIMATES

47. The transport rehabilitation program should be implemented through a Project Implementation Unit (PIU) linked to UNMIK. The PIU would assist UNMIK in dealing with transport issues in Kosovo. The PIU's task would be to advise UNMIK on transport policy issues, and to ensure an optimal use of donor resources allocated to the transport sector. It is proposed that a donor be sought to administer support for, and to monitor, the PIU. It is proposed to leave, under supervision of the PIU, the daily implementation of the transport rehabilitation program to the respective existing and emerging organizations (Road Organization, Railways, Airport Administration, etc.) which would be in charge of: (i) processing procurement and disbursement of rehabilitation contracts; (ii) supervising works progress; (iii) keeping up to date the list of priority works to be carried out under the program; and (iv) assisting UNMIK in carrying out the overall implementation of the program.

**Table 1: External Financing Requirements for the Transport Sector
(in millions of US dollars)**

Activity ⁴	First Phase (until December 2000)			Second Phase (2001-2003)	Total
	Until March 2000	April to Dec. 2000	Total		
INVESTMENTS					
Road Sector	4.1	39.9	44.0	84.0	128.0
Railways Sector	2.1	0.9	3.0	0.0	3.0
Public Transport Sector	0.0	1.0	1.0	1.0	2.0
Civil Aviation Sector	5.1	9.9	15.0	5.0	20.0
Subtotal	11.3	51.7	63.0	90.0	153.0
TECHNICAL ASSISTANCE					
Road Sector	0.0	0.3	0.3	0.2	0.5
Railways Sector	0.1	0.1	0.2	0.0	0.2
Public Transport Sector	0.0	0.1	0.1	0.2	0.3
Civil Aviation Sector	0.1	1.9	2.0	4.0	6.0
Project Management	1.0	2.0	3.0	2.0	5.0
Subtotal	1.2	4.4	5.6	6.4	12.0
Total⁵	12.5	56.1	68.6	96.4	165.0

⁴ Commitments have recently been made for some of the activities listed in this table.

⁵ In addition, about US\$1.14 million will have to be funded through the budget for operating expenditures in the sector. This includes US\$0.42 million for the period until December 2000.

ANNEX XI: MEETING IMMEDIATE NEEDS OVER THE NEXT THREE TO FOUR MONTHS

1. Current efforts are aimed at starting large-scale reconstruction and recovery activities in early Spring 2000. Before that, however, urgent action needs to be taken – both to prevent a humanitarian disaster during winter, and to pave the way for further, longer-term assistance programs. Continued support for the large scale humanitarian effort undertaken under UNHCR leadership is essential, in particular for providing food aid and basic supplies to the most needy, and for providing emergency shelter to those whose houses were destroyed. Significant amounts of assistance were pledged to that effect at the Donor Conference held on July 28, 1999.
2. Urgent needs, however, go beyond such requirements. Rapid action is needed to complement the humanitarian effort through: (i) a series of critical rehabilitation programs, mainly for the utilities networks and the social sectors, building on ongoing initiatives (particularly by UNMIK), to help ensure acceptable standards of provision of electric power, heat, clean water, and social services throughout the winter; and (ii) supporting the restart of agriculture.
3. Despite the collapse of institutions, and the loss of many archives and technical documents, detailed lists of requirements have been prepared by several international organizations (mainly KFOR, IMG, UN agencies, and UNMIK), a number of NGOs, and some bilaterals. Donors are encouraged to use these lists for financing urgent activities, but also to keep a degree of flexibility (without delaying critical activities), since updates and adjustments are expected as more information becomes available.
4. Prompt action is also necessary to allow for large-scale reconstruction and recovery activities to start next spring. Immediate requirements include: (i) preparing detailed projects ; (ii) passing key regulations which will enable further activities; and (iii) setting up critical institutions and systems (e.g., payment system) without which the implementation of major donor assistance will be very difficult. Donor support, mainly through technical assistance, will be essential for these tasks to be completed on time.
5. This annex outlines a number of critical requirements for the next three to four months in sectors which are key for economic recovery.¹ The corresponding financial requirements, for investment and technical assistance only, amounts to US\$217 million (see Table 1), which hopefully could be disbursed within the next few months.²
6. It is hoped that a large part of the urgent activities can be financed through pledges announced during the July 28 Donor Conference. In most cases, what is most urgently needed is a mechanism for quick decision-making, arranging the necessary financing, and putting in place appropriate implementation mechanisms. Normal procurement and other administrative procedures will largely have to be bypassed for this winter.

¹ Some donors have already announced their intention to finance some of the activities listed below.

² Additional support, estimated at US\$80 for the year 2000, is needed to complement these activities by filling the budgetary gap – so that operating expenditures can be funded at a proper level.

**Table 1 : Urgent Financing Requirements
(in millions of US dollars)**

Sector	Urgent Requirements
Agriculture	8
Private Sector Devt / Industry	16
Institutions	15
Housing	36
Water	30
Landmine clearing	7
Telecommunications	15
Energy	51
Transport	12
Education	11
Health	16
Total	217

Agriculture

Urgent Works and/or TA

- Continue providing farm inputs, including seeds, fertilizer, spare parts, and fuels (US\$6.0 million).
- Conduct a public livestock vaccination campaign against major contagious diseases to help safeguard the remaining animal stock in the province (US\$1.5 million).

Preparatory Activities

- Prepare large-scale rehabilitation programs for Spring 2000 (US\$0.5 million), including: (i) defining specific targeting criteria for replacement of assets, and identifying beneficiaries; (ii) setting up a coordination unit for implementation; and (iii) making advance arrangements with implementing agents (NGOs, municipal authorities and/or private contractors), including the design of a voucher program (and possibly the distribution of vouchers).

Private Sector Development

Urgent Works and/or TA

- Provide technical assistance to: (i) develop an enterprise privatization strategy and oversee its implementation; (ii) draft an enterprise law, a property rights framework, a commercial code, a bankruptcy law, a competition law, and an accounting law; and (iii) develop a lending strategy for small and medium-sized enterprises, including lending mechanisms (US\$4.0 million).
- Support the privatization program, including: (i) technical assistance for formulating specifics of the program (US\$0.5 million); (ii) an extensive public debate and information campaign on the privatization strategy (US\$0.8 million); (iii) initiation of privatization of

agro-processing and construction materials enterprises (US\$3.0 million); and (iv) the designing of a pilot program for privatization of about ten large enterprises (US\$5.0 million).

Institutions

- Needs are being identified by UNMIK and the EC Task Force in Kosovo (TAFKO). The US\$15 million provisional estimate corresponds to costs related to: (i) provision of equipment to the police, as per a list developed by the UN Police Commissioner (US\$9.7 million); (ii) minimal rehabilitation of key public buildings (US\$2.3 million); and (iii) technical assistance for the development of institutions (US\$3.0 million).

Housing

Urgent Works and/or TA

- Finance small-scale permanent rehabilitation works whenever possible, in complement to the UNHCR-led winterization program. The desired amount of work by far exceeds Kosovo's implementation capacities during the coming months. Works that can be carried on during this period have tentatively been estimated at US\$35 million.
- Initiate legal and regulatory work on the (re)registration of ownership where records have been lost or destroyed, as well as for collective housing ownership and management (US\$0.1 million).

Preparatory Activities

- Prepare large-scale rehabilitation programs for Spring 2000 (US\$0.4 million), including: (i) defining specific targeting criteria and identifying beneficiaries; (ii) setting up a coordination unit, developing agreed minimum and maximum rehabilitation standards and sharing work between donors; (iii) pre-positioning building materials and making advance arrangements with implementing agents (NGOs, municipal authorities and/or private contractors), including the design of a voucher program (and possibly the distribution of vouchers).

Water and Waste Collection

Urgent Works and/or TA

- Provide vehicles, tools, spares, pipes and fittings to the water supply entities for completing the most urgent repair works, as well as chemicals for flocculation and chlorine for disinfection (US\$15 million). Complete the rural well cleaning program currently underway (US\$3 million). Detailed lists of goods are being prepared by IMG and are expected to be available by December 1999.
- Provide equipment for solid waste management: (i) in Prishtine: 15 to 20 vehicles for solid waste collection (packers and dump trucks), 1,000 one m3 bins, 200 five to seven m3 bins, and one bulldozer for the landfill (US\$1.5 million); (ii) in other cities: 50 vehicles (packers and dump trucks), 1,000 five to seven m3 containers (US\$5.0 million); and (iii) an incinerator for medical waste (US\$1.5 million).

- Support the management of both water supply and solid waste management entities, as well as the restart of billing and collection for water through technical assistance (US\$2.1 million).

Preparatory Activities

- Launch a major feasibility study (or several complementary studies), to assess detailed investment requirements in each of the seventeen water systems, design least-cost solutions, and make recommendations, financing plans, water and waste tariffs, and consolidation of water supply systems (US\$2.0 million).

Mine-clearing

Urgent Works and/or TA

- Provide continued support to the ongoing effort, by extending funding to those current activities which are deemed effective by the UNMACC, including: level-two surveys (US\$3.0 million), clearing in inhabited areas and quality assurance (US\$2.0 million), mine awareness and dissemination of information currently available at UNMACC (US\$0.8 million), mine victim assistance (US\$0.3 million), and support to the UNMACC (US\$0.9 million).

Education

Urgent Works and/or TA

- Winterize primary and secondary schools in an effort to provide a minimally acceptable learning environment for children during the 1999-2000 school year. Recurrent funding would provide for heating which is essential to allowing schools to operate in Kosovo (US\$5.0 million). Detailed lists of needs are being prepared by UNICEF and IMG.
- Pilot a new education budgeting procedure which gives municipalities responsibility for setting education spending priorities, while introducing efficiency incentives through a focus on block grant per-student funding (US\$0.4 million)
- Design and set up a re-training fund for delivery of complementary education and professional training to adults, which requires technical assistance (US\$0.3 million) and financial support for start-up of the fund (US\$7.0 million).

Preparatory Activities

- Prepare a school reconstruction project, to be launched in Spring 2000, and in particular: (i) prepare technical designs for schools identified by UNMIK as priorities; and (ii) support the setting up of a central coordination unit within UNMIK to maximize use of donor funding (US\$0.3 million).
- Expose professional and managerial staff to Western European systems, institutions, and standards (e.g., curricula, university management and governance) through study tours and training (US\$0.5 million).

Health

Urgent Works and/or TA

- Re-start a widespread immunization program (US\$1.0 million).
- Conduct minor emergency repairs on health buildings, with a focus on primary health care facilities in rural areas, and provide basic medical equipment (US\$3.0 million). Detailed lists of needs are being prepared by WHO and IMG.
- Replace essential and emergency equipment including at the six main hospitals; replace essential immunization and public health equipment and provide technical assistance for communicable disease control and environmental health (US\$8.0 million).
- Re-start a Health Insurance Fund, including: (i) provision of adequate premises, equipment and office supplies (US\$1.5 million); (ii) provision of technical assistance (US\$1.5 million) to review the current regulatory framework, propose adjustments as needed, and define the main elements of health finance system (budgeting, revenue collection, expenditure allocation, and provider payment).

Preparatory Activities

- Prepare a health reconstruction project, to be launched in Spring 2000, and in particular: (i) prepare technical designs for health facilities identified by UNMIK as priorities, after a review of existing capacities and population needs; and (ii) support the setting up of a central coordination unit within UNMIK to maximize use of donor funding (US\$1.0 million).

Telecommunications

Urgent Works and/or TA

- Conduct a series of emergency repairs including: microwave repairs (US\$6.0 million), replacement of tandem switch (US\$2.0 million); initial rehabilitation of local networks and Pristine local exchange (US\$2.0 million); supply of spares, tools and testing devices (US\$2.0 million); and provisions of maintenance vehicles (US\$2.0 million).
- Provide technical assistance to help address legal issues, including: (i) licensing of GSM; and (ii) status and conditions for operations of the telecommunications company (US\$0.5 million).

Energy

Urgent Works and/or TA

- Ensure adequate availability of electric power through the winter by: (i) carrying out urgent repairs on Kosovo B (US\$6.6 million); procuring essential spare parts, consumables, and tools for the Kosovo A and B thermal power plants (US\$1.2 million); procuring mazut, diesel and chemicals required for the operation of the thermal power plants (US\$5.1 million); procuring essential spare parts and tools for the Gazivode hydropower plant, and arranging for necessary repairs (US\$0.2 million) – detailed lists of

goods and services required are being updated by UNMIK; (ii) negotiating arrangements with neighboring countries for import of power; and (iii) designing an appropriate load-shedding plan to manage excessive demand and/or shortfalls in domestic generation or electricity imports.

- Rehabilitate parts of the transmission and distribution networks, with a focus on principal substations (US\$1.3 million); major transmission lines (US\$0.1 million); and distribution networks (US\$15.0); provision of vehicles, tools, and equipment for maintenance of the transmission (US\$0.8 million) and distribution (US\$1.6 million) networks – detailed lists have been prepared by IMG and DFID.
- Enable the coal mines of Mirash and Bardh to produce sufficient coal for the thermal power plants during the coming winter by: providing bulldozers and other auxiliary equipment for the coal mines (US\$5.3 million); procuring essential spare parts, tools, safety items, fuels and lubricants (US\$0.5 million); and arranging for necessary repairs to the coal transport system (US\$0.1 million).
- Refurbish and reconnect district heating systems in Prishtine (US\$0.5 million), Gjakova (US\$0.1 million), and Mitrovica (US\$0.4 million); provide sufficient fuel (mazut) for the winter (US\$5.3 million); and procure essential spare parts, and arrange for necessary repairs (US\$1.0 million).
- Initiate cost recovery: restoration of billing and collection activities, procurement and installation of meters (total estimated requirement is for 150,000 meters, of which 50,000 should be ordered by spring 2000), analysis and control of cost of services, and review of tariff structures (US\$5.0 million).

Preparatory Activities

- Provide technical assistance to prepare a comprehensive energy sector rehabilitation project, to be launched in spring 2000 (US\$0.5 million).
- Conduct environmental audits for the power plant and associated mine (US\$0.1 million).

Transport

Urgent Works and/or TA

- Provide equipment for winter maintenance of the road network, including snow ploughs, trucks, and salt spreaders, as well as about 2,000 tons of salt and 2,000 tons of sand (US\$4.1 million).
- Allow for restart of civilian flights to Prishtine, through: (i) provision of ICAO-compliant aeronautical ground lighting (AGL); (ii) replacement of floodlights at the parking apron and installation of additional floodlight masts; (iii) replacement of the existing ILS; and (iv) pavement works on the runway and taxiway, including treatment of joints and cracks in the surface, repair of distressed asphalt, surface treatment (US\$5.1 million).
- Rehabilitate the Kosovo Polje railways workshop and loading ramp (US\$2.1 million).

Preparatory Activities

- Provide technical assistance to prepare a comprehensive transport sector rehabilitation project, to be launched in spring 2000 (US\$0.3 million).